Supreme Court U.S.
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In The

Supreme Court of the United States

October Term, 1996

IN THE MATTER OF TEXAS COMMERCE BANK-SAN ANGELO, N.A., AND TEXAS COMMERCE BANK-AUSTIN, N.A.,

Petitioners,

v.

BILLY R. SHURLEY AND JANE BRYANT SHURLEY,

Respondents.

On Petition For Writ Of Certiorari To The United States Court Of Appeals For The Fifth Circuit

PETITION FOR WRIT OF CERTIORARI

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88 pp

QUESTIONS STATED

Question 1.

Whether the Fifth Circuit's "novel" conclusion that creditors in bankruptcy can reach only what a settlor/beneficiary pays for an interest in a self-settled trust, rather than the beneficiary's entire interest in the trust, conflicts with the First Circuit's decision in *Spelinhauer v. Spencer Press, Inc.*, 101 F.3d 106 (1st Cir. 1996), *affirming*, 195 B.R. 543 (D.Me. 1996), *affirming*, 182 B.R. 361 (Bankr.D.Me. 1995).

Question 2.

Whether the Fifth Circuit's erroneous application of the Bankruptcy Code, 11 U.S.C. § 541(a), which states that an individual's bankruptcy estate includes all assets that may be reached by the individual's creditors in satisfying a judgment, amounts to both bad law and bad policy?

LIST OF PARTIES

Parties to the Case

1. Appellant Jane Bryant Shurley, Debtor

2. Appellant Billy R. Shurley, Debtor

3. Appellant William Armstrong II, Trustee of the M.D. Bryant Family Trust

4. Appellee Dennis L. Elam, Chapter 7 Bankruptcy Trustee

5. Appellee Texas Commerce Bank National Association

6. Appellee Texas Commerce Bank-San Angelo, National Association

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LIST OF PARTIES – Continued

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LIST OF PARTIES – Continued

Other Interested Parties

There are other relatives of Mrs. Shurley and remote or contingent beneficiaries of the M.D. Bryant Family Trust whose interests are fully represented by Appellant Armstrong.

29.1 STATEMENT

Chase Manhattan Corporation, a publicly held corporation, is the parent corporation of Texas Commerce Equity Holdings, Inc., which is not a publicly held corporation.

Texas Commerce Equity Holdings, Inc., in turn, is the parent corporation of the two petitioners, Texas Commerce Bank National Association, which has numerous subsidiaries, and Texas Commerce Bank-San Angelo, National Association, which has no subsidiaries.

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PETITION FOR WRIT OF CERTIORARI

Petitioners Texas Commerce Bank-San Angelo, N.A., and Bank-Austin, N.A., respectfully request that the Court grant the Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit.

OPINIONS BELOW

Petitioners' Appendices provide the pertinent opinions.

JURISDICTION

Jurisdiction exists under 28 U.S.C. § 1254.

STATUTORY AND REGULATORY PROVISIONS INVOLVED

Petitioners' Appendices provide the pertinent section of the Bankruptcy Code.

STATEMENT OF CASE

The United States Court of Appeals for the Fifth Circuit entered its opinion and judgment on June 20, 1997. Petitioners filed a motion for rehearing and a

suggestion of rehearing en banc,[1] which the Fifth Circuit denied on August 8, 1997.

The Petitioners are creditors in bankruptcy – Texas Commerce Bank-Austin, and Texas Commerce Bank-San Angelo ("the Banks").[2] Joined by the bankruptcy trustee, they filed an original adversary proceeding in bankruptcy court in which they asked the court to declare that the bankruptcy estate included the full extent of the Respondent's interest in the M.D. Bryant Family Trust – a protective trust that the Respondent, Mrs. Shurley, her sister, and her parents created more than thirty years earlier.

Despite the protective language in the trust, the bankruptcy court found that Mrs. Shurley's interest in the trust was part of the bankruptcy estate because Mrs. Shurley self-settled the trust, and because she exerted extensive control over, and manipulation of, the trust assets. Consequently, the bankruptcy court found that the bankruptcy trustee was entitled to reach Mrs. Shurley's "interest" in the Trust, which is "the maximum amount which the trustee under the terms of the trust could pay to [Mrs. Shurley] or apply for her benefit." RESTATEMENT OF TRUSTS (SECOND) § 156(2); *Spenlinhauer v. Spencer Press, Inc.*, 195 B.R. 543 (Bankr. D.C. Maine 1996), *aff'd*, 101 F.3d 106 (1st Cir. 1996). Under the Trust Agreement, the trustees can give Mrs. Shurley up to one-half of the total trust assets. Consequently, the bankruptcy court entered judgment for half of the trust assets, and the United States

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[1] The Fifth Circuit also denied Petitioner's motion to certify the state law question to the Texas Supreme Court.

[2] Dennis Elam – the Chapter 7 Trustee and a plaintiff-appellee in the court of appeals – does not join in this petition.

District Court for the Western District of Texas affirmed. On further appeal, the United States Court of Appeals for the Fifth Circuit reversed in part, concluding that Mrs. Shurley's creditors could reach – not Mrs. Shurley's one-half interest in the trust – but only her initial investment, made some thirty years earlier – the Marfa Ranch.[3]

The Fifth Circuit's conclusion is both bad policy and bad law, and directly conflicts with a recent First Circuit case with similar facts. *See Spenlinhauer v. Spencer Press, Inc.*, 182 B.R. 361 (Bankr.D.Me. 1995, 195), *aff'd*, 195 B.R. 543 (D.Me. 1996), *aff'd* 101 F.3d 106 (1st Cir. 1996). For these reasons, Petitioners ask the Court to exercise its certiorari jurisdiction and resolve the conflict between the Circuits, and settle an important question of federal bankruptcy law – the extent to which a self-settled trust can be reached as part of the bankruptcy estate.

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[3] The settlors of the M.D. Bryant Family Trust, created in 1965 by Trust Deed, were Mrs. Shurley's parents – M.D. and Ethel Bryant – and Mrs. Shurley and her sister, Anne Bryant Watkins. Mrs. Shurley's contribution to the trust res was the Marfa Ranch, a 10,947 acre tract in Presideo County. According to the Trust Deed, Mrs. Shurley and her sister each contributed 1/6th of the trust estate, while their parents contributed the remaining two-thirds. On the death of M.D. and Ethel Bryant, the sisters became equal, one-half lifetime beneficiaries.

REASONS FOR GRANTING THE WRIT

A. This is an appropriate case in which to grant the writ in order to correct the conflict between the well-established law of the First Circuit, and other Circuits, and the Fifth Circuit's erroneous and dangerous conclusion that a beneficiary's interest in a self-settled trust is the same as the consideration that the beneficiary pays for that interest.

According to the Fifth Circuit, "[t]he novel issue presented here is whether the entirety of a beneficiary's interest in a spendthrift trust is subject to creditors' claims where the trust is only partially self-funded by the beneficiary." This issue is indeed "novel." Petitioners are unaware of any other court that has considered the matter as anything other than well-settled that a "settlor/beneficiary's 'interest' is "the maximum amount which the trustee under the terms of the trust could pay to [the beneficiary] or apply for his benefit." RESTATEMENT OF TRUSTS (SECOND) § 156(2); *In re Robbins*, 826 F.2d 293 (4th Cir. 1987); *In re Morris*, 144 B.R. 401 (Bkrtcy C.D. Ill. 1992, *aff'd*, 151 B.R. 900 (C.D. Ill. 1993)). This so-called "novel" issue should not arise because only a beneficiary, not a settlor, has an "interest" in a trust. A settlor "contributes" or "delivers" property to the trust, but has no "interest" other than what he or she retains as a beneficiary. Mrs. Shurley traded the Marfa Ranch for a beneficial interest in the Trust. As such, her creditors can reach what Mrs. Shurley "bought" – not what she "paid" for that interest.

Because the Fifth Circuit raised, and incorrectly determined, an issue that should never arise, it had to acknowledge a lack of authority for its conclusion that a beneficiary's interest in a trust is somehow limited by the

beneficiary's initial contribution to the trust more than thirty years earlier.[4] In fact, the court cites only an intermediate Michigan appellate court opinion, which is clearly distinguishable, in support of its conclusion. *See In re Johannes Trust*, 191 Mich. App. 514 N.W.2d 25, 29 (1991).[5] Indeed, the pertinent authority is precisely counter to the Fifth Circuit's decision. *See Spenlinhauer v. Spencer Press, Inc.*, 182 B.R. 361 (Bankr.D.Me. 1995, 195), *aff'd* B.R. 543 (D.Me. 1996), *aff'd* 101 F.3d 106 (1st Cir. 1996).

In *Spenlinhauer*, three brothers formed a trust, containing a spendthrift clause, for their mutual benefit. All three were considered by the court to be both settlors and beneficiaries. 195 B.R. at 544. The court concluded that, because the trust was self-settled, the debtor's *entire interest* in the trust was part of the bankruptcy estate – a conclusion that is precisely counter to the Fifth Circuit's holding here. *Id.* at 544.

Because of the need for careful long-term planning, certainty and stability are essential in this area of the law. Rather than promoting stability, the Fifth Circuit's decision creates confusion, uncertainty, and a split in authority with the First Circuit. Consequently, the Fifth Circuit's

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[4] The Fifth Circuit would use as a measure of recovery the same assets that Mrs. Shurley initially transferred to the trust and which she testified that she never expected to get back.

[5] The portion of the *Johannes Trust* opinion on which the Fifth Circuit relied was dictum both because the trust was not a spendthrift trust, and because the court could not tell whether the trust was a multiple settlor trust. In fact, the trust was entirely self-settled by the funds of the beneficiary (placed in trust by her guardian with court approval).

renegade ruling is especially dangerous, and Petitioners respectfully request that this Court grant the writ, reverse the Fifth Circuit, and affirm the bankruptcy court.

B. This is an appropriate case in which to grant the writ because it involves an important question of federal bankruptcy law – the extent to which a beneficiary's interest in a self-settled trust becomes part of the bankruptcy estate.

The Panel's "novel" conclusion that a creditor can reach only the consideration that a settlor/beneficiary pays for his or her interest in a self-settled trust is both bad policy and bad law. According to the Fifth Circuit, Mrs. Shurley's interest in the Trust is the Marfa Ranch. It is not. The Marfa Ranch is the consideration that Mrs. Shurley paid in 1965 for her interest in the Trust. That interest ripened into her one-half share approximately twenty years *before* she filed bankruptcy.

As a matter of federal statute, an individual's bankruptcy estate includes all assets that may be reached by the individual's creditors in satisfying a judgment. 11 U.S.C. § 541(a); *see Sierra Switchboard Co. v. Westinghouse Elec. Corp.*, 789 F.2d 705, 707 (9th Cir. 1986); *Tignor v. Parkinson*, 729 F.2d 977, 980 (4th Cir. 1984); *Cowan v. Fidelity Interstate Life Ins. Co.*, 89 Bankr. 564, 571 (E.D. La. 1988). According to the trust instrument and the bankruptcy court's unchallenged fact findings, the trustee can provide Mrs. Shurley with 50% of all corpus assets. (*See* T.I. pp. 2, 4 (b) and (e)). Thus, the Fifth Circuit's creation of a bogus issue – whether Mrs. Shurley's interest in the

trust was somehow limited by her initial contribution – amounts to a basic misconstruction of federal law.

The Panel's decision is also bad policy because it makes the amount of the trust that a creditor can reach depend on the vicissitudes of the trustee's investment decisions, which could produce unfortunate results for innocent beneficiaries, and because creditors cannot depend upon the terms of the pertinent documents. The Fifth Circuit's decision also requires the bankruptcy and district courts to undergo a complex tracing analysis that not only will place an exceptional burden on these courts, but, in many cases, will be impossible to perform.

For example, the Fifth Circuit's "novel" rule will be nearly impossible to apply where the property that the beneficiary initially contributed has, through the vicissitudes of the trustee's investment policy, substantially changed over a long period of time. For example, had the Marfa Ranch been sold years ago, the court could face a nearly impossible burden of having to value a decades old trust contribution. In fact, part of Mrs. Shurley's initial contribution was in the form of mineral interests (V. 23-1655), the proceeds of which may be impossible to trace at this point.

The Fifth Circuit apparently articulated its "novel" rule in a misguided attempt to do equity. According to the Fifth Circuit, allowing creditors to reach Mrs. Shurley's 50% interest in the trust "ignores the wishes of Shurley's parents, the primary settlors of the trust, and the state's policy of respecting their expectations." Slip. Op. at 3610. Rather than producing an equitable result,

however, the panel rule would, in many instances, produce results that no right-thinking person would tolerate. For example, the property contributed by a co-settlor/beneficiary could disproportionately increase in value, in which case, if that co-settlor/beneficiary declared bankruptcy, a disproportionate, and often inequitable portion of the trust's assets, would become part of the bankruptcy estate. For example, if a settlor/beneficiary has only a fifty percent interest in the trust, but the property that the settlor/beneficiary contributed now accounts for ninety-eight percent of the trust assets, creditors should not be able to reach ninety-eight percent of the trust assets.

The Fifth Circuit's rule could also lead to inconsistent results depending on whether assets in a particular case are retained or sold, and if retained, whether their value goes up or down. Assume, for example, that two brothers (A and B) established a trust in 1950, which provided equal interests for them and otherwise had the same provisions as the M.D. Bryant Family Trust Under the Panel's Opinion, the spendthrift provision would be invalid. Suppose, further, that A contributed $10,000 worth of IBM stock and B contributed an equivalent amount of some other company's stock which subsequently became worthless (Studebaker Motor Company, for example). In 1992, one of the brothers declares bankruptcy. Under the correct rule of law, the result with respect to the brothers' creditors would be the same no matter which one declares bankruptcy. Under the panel's approach, however, if the bankrupt brother is B, his creditors would get nothing, and he would remain a 50% beneficiary of a multi-million dollar trust; if the bankrupt brother is A, his creditors would receive virtually the

entire trust, wiping out the interest of B (not in bankruptcy), along with A.

The Fifth Circuit's ruling is also bad bankruptcy law because creditors, or persons about to extend credit, will not be able to depend on the validity of the trust instrument. Here, the deeds that conveyed property into the Trust are unqualified conveyances – without reservation if the spendthrift provision proves to be invalid. Creditors should be able to rely on their examination of the relevant documents, especially where, as here, a debtor lists the Trust assets on his or her financial statement. (V. 24-1842-1843). Because the Fifth Circuit's erroneous application of federal bankruptcy law sets a dangerous and unfortunate precedent, Petitioners respectfully ask the Court to grant writ of certiorari and reverse the court of appeals.

CONCLUSION

The Fifth Circuit's "novel" conclusion that creditors are limited to the consideration that a settlor/beneficiary pays for his or her interest in a trust is both bad policy and bad law. It injects uncertainty and confusion into an area of the law in which certainty and stability are critical. The Fifth Circuit's decision is also bad policy because it requires a complex tracing analysis that will often be impossible to perform, because it makes the amount of the trust that a creditor can reach depend on the vicissitudes of the trustee's investment decisions, which could produce unfortunate results for innocent beneficiaries, and because creditors cannot depend upon the terms of

the pertinent documents. For these reasons, Petitioners ask the Court to grant writ of certiorari, reverse the Fifth Circuit Court of Appeals, and affirm the bankruptcy court.

Respectfully submitted.

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APPENDIX 1

In The Matter of Billy R. SHURLEY and Jane Bryant Shurley, Debtors.

Billy R. SHURLEY and Jane Bryant Shurley, Appellants,

v.

TEXAS COMMERCE BANK – AUSTIN, N.A. and Texas Commerce Bank – San Angelo, N.A., Appellees.

In The Matter of Billy R. SHURLEY and Jane Bryant Shurley, Debtors.

Billy R. SHURLEY and Jane Bryant Shurley, Appellants,

v.

TEXAS COMMERCE BANK – SAN ANGELO, N.A., Texas Commerce Bank – Austin, N.A. and Dennis Elam, Trustee, Appellees.

In The Matter of Billy R. SHURLEY and Jane Bryant Shurley, Debtors.

William H. ARMSTRONG, II, Appellant,

v.

TEXAS COMMERCE BANK – SAN ANGELO, N.A., Dennis Elam, Trustee, and Texas Commerce Bank – Austin, Appellees.

Nos. 96-50137, 96-50138.

United States Court of Appeals,
Fifth Circuit.

June 20, 1997.

Creditors and Chapter 7 trustee filed adversary proceeding against debtors and trustee of family trust, in which creditors and trustee sought declaratory judgment

that debtor's interest in trust was included in property of her bankruptcy estate. The United States Bankruptcy Court for the Western District of Texas, Ronald B. King, J., 171 B.R. 769, entered judgment in favor of plaintiffs, and trustee of family trust appealed. The District Court, David Briones, J., affirmed. On further appeal, the Court of Appeals, Reavley, Circuit Judge, held that: (1) under Texas self-settlor rule, property which Chapter 7 debtor herself contributed to spendthrift trust established by debtor, her parents and sister was not protected from claims of creditors, and was therefore included in "property of the estate"; (2) control granted to debtor over trust pursuant to terms of trust agreement was not sufficient to bring other assets of trust within property of the estate; (3) fact that trustees of spendthrift trust liberally bestowed trust assets on debtor, in manner on its face consistent with purpose and language of trust, was not sufficient to establish debtor's de facto control over affairs of trust, so as to bring trust assets within debtor's bankruptcy estate; and (4) debtor's interest in trust could be characterized as "annuity," which debtor could claim as exempt pursuant to special Texas exemption for debtor's interest in annuity contract.

Reversed and remanded.

Appeals from the United States District Court for the Western District of Texas.

Before REAVLEY, JOLLY and BENAVIDES, Circuit Judges.

REAVLEY, Circuit Judge:

The question here is to what extent the assets of a spendthrift trust settled by a bankruptcy debtor and others are included in the debtor's bankruptcy estate. The bankruptcy and district courts held that the entirety of the debtor's interest in the trust is property of the bankruptcy estate. We limit the estate to the property contributed to the trust by the debtor.

BACKGROUND

In 1965 M.D. Bryant, Ethel Bryant, Anne Bryant Ridge, and Jane Bryant Shurley created a trust under Texas law. M.D. and Ethel Bryant were husband and wife. Anne Bryant Ridge and Jane Bryant Shurley are their daughters. The trust is known as the "M.D. Bryant Family Trust" or the "Bryant Family Trust."

The parents and daughters contributed real property to the trust. The property consisted of ranches owned by the family, including one owned by Shurley. Shurley contributed approximately 11,000 acres of raw land from the south of a west Texas ranch (her contribution herein the "Marfa ranch").[1] The trust agreement states that the property contributed by the parents "represents two-thirds (2/3) of the total value of all of said real property to be contributed and that the value of that portion of said real property to be contributed by [the two daughters]

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[1] The briefs indicate that the "Marfa Ranch" also refers to a larger tract of land out of which came the acreage Shurley contributed to the trust. In this opinion the "Marfa ranch" means only that acreage owned by Shurley and conveyed to the trust in 1965, together with any mineral interests she may have owned and conveyed to the trust.

each represents (1/6) of the total value of all of said real property to be contributed."

The trust agreement provided that additional property could be added to the trust at a later date. According to Shurley the vast bulk of the corpus of the trust came through pourover provisions in the parents' wills, which were executed at the same time the trust agreement was executed. She claims that the Marfa ranch represents only two percent of the value of the total assets of the trust. The parents died in 1967 and 1971.

Under the trust agreement, while the parents were alive, two-thirds of the income generated by the trust was distributed to the parents and one-sixth of the income was distributed to each of the daughters. Upon the death of one parent, the income was distributed equally among the living parent and the daughters. Upon the death of the second parent, the two daughters each received half of the income if both were living at the time. The agreement has provisions for the children and other descendants of the daughters to receive income from the trust and distribution of its assets upon final termination of the trust.

In 1992, Shurley and her husband filed for bankruptcy under Chapter 7 of the Bankruptcy Code. Since Shurley's parents were deceased at the time, she and her sister each had a one-half interest in the income from the trust. The Marfa ranch was still held by the trust. Two bank creditors and the bankruptcy trustee brought an adversary action, seeking a declaratory judgment that Shurley's interest in the trust was property of the bankruptcy estate. After a trial, the bankruptcy court entered a

judgment declaring that Shurley's "entire interest in the [trust], being an undivided 50 percent interest in the principal assets and income of the [trust], is property of the Chapter 7 bankruptcy estate." In its memorandum opinion it enjoined the trustee of the trust "from disbursing any beneficial interest previously held by Mrs. Shurley to anyone other than" the bankruptcy trustee.[2] Shurley and the trustee of the trust[3] appealed to the district court, which affirmed. This appeal followed.

DISCUSSION

We review the bankruptcy court's factual findings under the clearly erroneous standard, and we review its legal conclusions de novo.[4]

Under section 541 of the Bankruptcy Code[5] a bankruptcy estate is created at the commencement of the bankruptcy case. Section 541(a)(1) states that "[e]xcept as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case" is included in the estate. Subsection (c)(2) states the exclusion relevant here: "A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title."

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[2] *In re Shurley*, 171 B.R. 769, 789 (Bankr.W.D.Tex.1994).

[3] For convenience, appellants Shurley and the trustee of the trust are sometimes collectively referred to as Shurley.

[4] *In re Herby's Foods, Inc.*, 2 F.3d 128, 130-31 (5th Cir.1993).

[5] 11 U.S.C. § 541.

Section 541(c)(2) excludes "spendthrift trusts" from the bankruptcy estate if such a trust protects the beneficiary from creditors under applicable state law.[6] "In general, a spendthrift trust is one in which the right of the beneficiary to future payments of income or capital cannot be voluntarily transferred by the beneficiary or reached by his or her creditors."[7]

The Bryant Family Trust agreement vests in the trustee authority over the trust assets. Among other powers vested in the trustee, the agreement provides:

> The trustee (and his successors) shall have full power and authority: to manage, handle, invest, reinvest, sell for cash or credit, or for part cash and part credit, convey, exchange, hold, dispose of, lease for any period of time, whether or not longer than the life of the trust, improve, repair, maintain, work, develop, operate, use, mortgage, or pledge all or any part of the funds. . . . The trustee shall have full power to determine the manner in which expenses are to be borne and in which receipts are to be credited as between principal and income, and also to determine what shall constitute income or net income and what shall constitute corpus and

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[6] *Patterson v. Shumate*, 504 U.S. 753, 762, 112 S.Ct. 2242, 2248, 119 L.Ed.2d 519 (1992) (noting legislative history that § 541(c)(2) "continues over the exclusion from property of the estate of the debtor's interest in a spendthrift trust to the extent the trust is protected from creditors under applicable State law."); *In re Moody*, 837 F.2d 719, 722-23 (5th Cir.1988) ("A beneficiary's interest in a spendthrift trust is excluded from his bankruptcy estate by 11 U.S.C. § 541(c)(2), if state law and the trust so provide.").

[7] *Id.* at 723.

> principal. . . . [B]eneficiaries shall have no right or power to transfer, assign, convey, sell or encumber said trust estate and interest therein, legal or equitable, during the existence of these trusts.

The agreement expressly provides that trust assets cannot be reached by creditors of the beneficiaries.[8]

By vesting control of the trust in the trustee, denying the beneficiaries control over the trust, and denying creditors of the beneficiaries access to trust assets, the trust agreement qualifies as a spendthrift trust under Texas law. For two reasons, however, the bankruptcy court concluded that the trust assets are not beyond the reach of creditors under state law. The first reason, which we reject in part, is that spendthrift trust protection under state law does not extend to a trust settled by the beneficiary herself. The second reason, which we reject, is that Shurley exercised sufficient control over the trust to make the assets subject to her creditors.

---

[8] The agreement states: "The interest of the beneficiaries in the trust estate and the increase and proceeds thereof, both legal and equitable, so long as the same are held in trust, shall not be subject in any manner to any indebtedness, judgment, judicial process, creditors' bills, attachment, garnishment, execution, receivership, charge, levy, seizure or encumbrance, of or against said beneficiaries; nor shall the interest of the beneficiaries in said trust be in any manner reduced or affected by any transfer, assignment, conveyance, sale, encumbrance, act, omission or mishap, voluntary or involuntary, anticipatory or otherwise of said beneficiaries. . . . "

A. *The Self-Settlor Rule and its Consequences*

The bankruptcy court's principal reason for holding that Shurley's interest in the trust is property of the bankruptcy estate is that she was one of the original settlors of the trust. We have recognized that a beneficiary's interest in a spendthrift trust is not subject to claims of creditors under Texas law "[u]nless the settlor creates the trust and makes himself beneficiary."[9] The rationale for this "self-settlor" rule is obvious enough: a debtor should not be able to escape claims of his creditors by himself setting up a spendthrift trust and naming himself as beneficiary. Such a maneuver allows the debtor, in the words of appellees, to "have his cake and eat it too." As one Texas court has explained:

> Public policy does not countenance devices by which one frees his own property from liability for his debts or restricts his power of alienation of it; and it is accordingly universally recognized that one cannot settle upon himself a spendthrift or other protective trust, or purchase such a trust from another, which will be effective to protect either the income or the corpus against the claims of his creditors, or to free it from his own power of alienation. The rule

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[9] *Id.* at 723. *See also Daniels v. Pecan Valley Ranch, Inc.*, 831 S.W.2d 372, 378 (Tex.App. – San Antonio 1992, writ denied) ("In Texas, a settlor cannot create a spendthrift trust for his own benefit and have the trust insulated from the rights of creditors."); Tex. Prop.Code Ann. § 112.035(d) ("If the settlor is also a beneficiary of the trust, a provision restraining the voluntary or involuntary transfer of his beneficial interest does not prevent his creditors from satisfying claims from his interest in the trust estate.").

> applies in respect of both present and future creditors and irrespective of any fraudulent intent in the settlement or purchase of a trust.[10]

The novel issue presented here is whether the entirety of a beneficiary's interest in a spendthrift trust is subject to creditors' claims where the trust is only partially self-funded by the beneficiary. There is no compelling Texas authority on this issue, but we conclude that on these facts Texas courts would surely hold that the partially self-funded spendthrift trust is only partially subject to creditors' claims.

Allowing creditors to reach only the self-settled portion of the trust is consistent with the other long-standing rule of Texas law that a settlor should be allowed to create a spendthrift trust that shields trust assets from the beneficiary's creditors. "Spendthrift trusts have long been held valid by Texas courts."[11] The bankruptcy court's ruling ignores the wishes of Shurley's parents, the primary settlors of the trust, and the state's policy of respecting their expectations. "Spendthrift trusts are not sustained out of consideration for the beneficiary. Their justification is found in the right of the donor to control his bounty and secure its application according to his pleasure."[12] Allowing creditors to reach only that portion of the trust contributed by Shurley would further the policy of allowing her parents to create a spendthrift trust

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[10] *Glass v. Carpenter*, 330 S.W.2d 530, 533 (Tex.Civ.App. – San Antonio 1959, writ ref'd n.r.e.).

[11] *Moody*, 837 F.2d at 723.

[12] *Hines v. Sands*, 312 S.W.2d 275, 279 (Tex.Civ.App. – Fort Worth 1958, no writ).

for the benefit of Shurley that is protected from her creditors, while giving effect to the exception for self-settled trusts. At least one court from another jurisdiction agrees with this approach,[13] and we believe that Texas courts would do the same. Accordingly we hold that the property which Shurley herself contributed to the trust – the Marfa ranch – is not protected from creditors under state law and is therefore property of the bankruptcy estate, but that all other assets of the trust are not property of the estate.[14]

We so hold despite Shurley's "power of appointment" granted by the trust agreement. Under the agreement each sister has a right to allocate assets of the trust to specified beneficiaries. The agreement states that the sisters "shall each have a special power of appointment over an adjusted one-half (1/2) of the trust assets, to

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[13] *In re Johannes Trust*, 191 Mich.App. 514, 479 N.W.2d 25, 29 (1991) ("[The self-settlor's] creditors can reach the assets of the trust and compel payment in the maximum amount that would be in the trustee's discretion with respect to that portion of the assets that came from [the self-settlor], but not with respect to any portion of the trust that came from other individuals, particularly petitioner.").

[14] We note that the Marfa ranch was still held by the trust when Shurley commenced her bankruptcy case. If the ranch had been sold, prior to the bankruptcy filing, this case would be more complicated. We would still hold that some portion of Shurley's interest in the trust was self-settled and therefore property of the estate, but would have to engage in a further analysis of (1) how to value the self-settled portion of the trust, through tracing of assets or some other method of calculating Shurley's proportionate contribution to the trust relative to the other settlors' contributions, and (2) who should have the burden of proof on this issue.

appoint such adjusted one-half (1/2) of the assets of said trust to and among their children and lineal descendants. . . . Neither [daughter] can appoint assets to herself, her creditors, her estate, or the creditors of her estate." If a daughter does not exercise her power of appointment, the trust agreement provides that her interest shall be distributed in equal shares "to her children and lineal descendants, and to the lineal descendants of a deceased child, per stirpes." Shurley represents on appeal that she has not exercised her special power of appointment because she is content with the trust's distribution provisions for her descendants.

This power of appointment does not alter our conclusion that the Marfa ranch is property of the bankruptcy estate. The Bankruptcy Code expressly excludes such a power of appointment from the bankruptcy estate, since section 541(b)(1) provides that property of the estate does not include "any power that the debtor may exercise solely for the benefit of an entity other than the debtor." However, while the *power* of appointment to others does not become property of the estate under § 541(b)(1), the *property* which became part of the bankruptcy estate under the Code upon the commencement of the bankruptcy case now belongs to that estate and is controlled by the bankruptcy trustee. Regardless of how Shurley might indicate that trust assets should be divided upon her death, the Marfa ranch now belongs to the bankruptcy estate, and her designation of beneficiaries is irrelevant. The bankruptcy estate will be divided among creditors according to the Code, regardless of Shirley's appointment of assets under the trust agreement.

The exercise of the power of appointment under the trust agreement is analogous to a will, and has no more effect on the property of the bankruptcy estate and creditor priorities than a garden-variety will of the debtor. With an ordinary will, the heirs only receive the stipulated items of the property that were owned by the testator. Stated more simply, a testator can only give away that which was hers. Here, the Marfa ranch no longer belongs to Shurley; it is property of the bankruptcy estate.

Shurley argues that she only has a life estate in the Marfa ranch and other trust assets in the form of an equitable interest in the income from the trust assets during her life, and that creditors therefore cannot reach the corpus of the trust even if it is self-settled. She is correct that absent distributions of corpus at the discretion of the trustee or a premature termination of the trust (discussed below), the trust agreement only provides her with an income interest in the trust assets, with the remainder going to other beneficiaries. Shurley cites authority that even when a settlor creates a trust for herself, creditors can only reach trust assets to the extent of the settlor's interest.[15]

The issue here – whether the creditors can reach only Shurley's income from the Marfa ranch or the ranch itself – does not turn on whether the Shurley's interest in the trust is "equitable," since the Bankruptcy Code defines property of the bankruptcy estate to include "all legal or

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[15] *E.g., Fordyce v. Fordyce*, 80 Misc.2d 909, 365 N.Y.S.2d 323, 328 (N.Y.Sup.Ct.1974) ("Even in the case of a self-settled trust, creditors can only reach the interest the settlor retained for himself.").

equitable interests of the debtor in property."[16] Resolution of this question turns on whether creditors can reach the trust corpus under state law, regardless of how the interest is characterized.

We conclude that under Texas law creditors can reach not only Shurley's income from the Marfa ranch but the ranch itself, in light of *Bank of Dallas v. Republic National Bank of Dallas.*[17] In *Bank of Dallas,* the debtor settled a trust with spendthrift language for the benefit of herself and her children. The debtor was to receive the net income of the trust during her lifetime, with the remainder going to her children or other beneficiaries named in her will. The trust agreement further provided that "[w]henever the trustee determines that the income of the Settlor from all sources known to the trustee is not sufficient for her reasonable support, comfort, and health and for reasonable support and education of Settlor's descendants, the trustee may in its discretion pay to, or use for the benefit of, Settlor or one or more of Settlor's descendants so much of the principal as the trustee determined to be required for those purposes."

The court held that "where a settlor creates a trust for his own benefit, and inserts a spendthrift clause, it is void as far as then existing or future creditors are concerned, and they can reach his interest under the trust by garnishment."[18] It further held that income from the trust was

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[16] 11 U.S.C. § 541(a)(1).

[17] 540 S.W.2d 499 (Tex.Civ.App. – Waco 1976, writ ref'd n.r.e.)

[18] *Id.* at 501.

subject to creditor claims, and that "the interest of [the debtor] in the trust is such that the corpus may be reached by her creditors."[19]

The court considered the Restatement (Second) of Trusts § 156 (1959), which provides:

> (1) Where a person creates for his own benefit a trust with a provision restraining the voluntary or involuntary transfer of his interest, his transferee or creditors can reach his interest.
>
> (2) Where a person creates for his own benefit a trust for support or a discretionary trust, his transferee or creditors can reach the maximum amount which the trustee under the terms of the trust could pay to him or apply for his benefit.

The court also looked to comment e of this section, which states that "[w]here by the terms of the trust a trustee is to pay the settlor or apply for his benefit as much of the income or principal as the trustee may in his discretion determine, his transferee or creditors can reach the maximum amount which the trustee could pay to him or apply for his benefit." Applying these rules the court held that the creditor could reach the corpus of the trust, even though the debtor only had a life interest in the trust.

By this reasoning the creditors are able to reach the self-settled asset of the trust in our case, namely the Marfa ranch. The trust agreement states that "[i]f the trustee determines that the net income of said trust is

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[19] *Id.* at 501-02.

insufficient to maintain and support any of the beneficiaries of said trust or their children and lineal descendants in their accustomed manner of living, taking into account, however, such beneficiary's income from all other sources, the trustee may use so much of the corpus of said trust as the trustee sees fit to make up such deficiency." This language is even broader than the language of the trust agreement in *Bank of Dallas*, since in our case the trustee can make grants of trust corpus to support the beneficiaries' or their descendants' "accustomed manner of living," while in *Bank of Dallas* the trustee was limited to making such distributions to support the beneficiary's "reasonable support, comfort, and health" and the reasonable support and education her descendants. If anything, the former term grants even more discretion to the trustee than the latter. Accordingly we conclude that the creditors in our case can reach the corpus of the trust under Texas law as to that property – the Marfa ranch – contributed by Shurley to the trust, and that the ranch is therefore property of the estate.

The court in *Bank of Dallas* also quoted comment c to § 156, which states that "[i]f the settlor reserves for his own benefit not only a life interest but also a general power to appoint the remainder by deed or will or by deed only or by will alone, the creditors can reach the principal of the trust as well as the income." In *Bank of Dallas* the debtor apparently had a general power to appoint the remaining trust assets by will, while in our case Shurley and her sister have a special power of appointment, meaning that the trust document limits the choice of recipients of appointed assets to the sisters' descendants. We do not see this factual distinction as

significant. Comment c was only one of three comments to § 156 (comments c, d, and e) quoted by the court in *Bank of Dallas*, and § 156 itself, as we read it, states than any self-settled support or discretionary trust is subject to creditor claims up to "the maximum amount which the trustee under the terms of the trust could pay to" the beneficiary. We cannot fathom why the court would have reached a different result if the debtor had had a special rather than a general power of appointment. Before even mentioning the Restatement, the court stated without qualification that, under Texas law, "where a settlor creates a trust for his own benefit, and inserts a spendthrift clause, it is void as far as then existing or future creditors are concerned, and they can reach his interest under the trust by garnishment."[20]

A similar result was reached in *State v. Nashville Trust Co.*[21] The debtor was the beneficiary of a spendthrift trust holding real estate. The debtor built a mansion on the property. The court held that the debtor had self-settled the trust to the extent of the improvements he had made, and that the property was therefore subject to the creditor's claim to the extent of the debtor's improvements. The debtor argued that even if he "can be held to have contributed to the trust property, enhanced its value, and to that extent created a spendthrift trust for his own benefit, only his interest in such enhancement, i.e. his life estate in such enhancement, may be subjected and that the remainder interest of his children . . . may not be

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[20] *Bank of Dallas*, 540 S.W.2d at 501.

[21] 28 Tenn.App. 388, 190 S.W.2d 785 (1944).

subjected for any debt of his."[22] The court rejected this argument, reasoning that the debtor's children "could only be donees or volunteers and could take no benefits under such transfer as against his creditors. So we think the chancellor did not err against defendants in decreeing that the [creditor] had a right to subject the land for the amount by which its value had been enhanced by reason of the improvements."[23] The court held that the creditor was entitled to a lien on the trust property for the value of the debtor's improvements, and that the creditor was "entitled to a sale of the land, if necessary, to enforce the lien."[24]

Shurley argues that creditors cannot reach the corpus of the trust because of our decisions in *In re Goff*, 706 F.2d 574 (5th Cir.1983) (*Goff I*), and *In re Goff*, 812 F.2d 931 (5th Cir.1987) (*Goff II*). In *Goff I* we held that the debtor's Keogh plan, a pension trust under the ERISA statute,[25] was not a spendthrift trust excluded from the bankruptcy estate under Bankruptcy Code § 541(c)(2) because it was self-funded. We stated that "[t]he general rule is well established that if a settlor creates a trust for his own benefit and inserts a 'spendthrift' clause, restraining alienation or assignment, it is void as far as creditors are concerned and they can reach the settlor's interest in the trust."[26]

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[22] *Id.* 190 S.W.2d at 791.

[23] *Id.* at 792.

[24] *Id.* at 799.

[25] 29 U.S.C. §§ 1001 *et seq.*

[26] *Goff I*, 706 F.2d at 587. The principal holding of the case – that a qualified ERISA pension plan is not excluded from the

In *Goff II*, a creditor claimed that its recorded judgment against the debtor gave it a statutory lien against the property held in the pension trust, and that it therefore had a secured bankruptcy claim. The bankruptcy trustee argued that the claim was unsecured. We held that the claim was unsecured, because under Texas law a judgment lien only attaches to real property in which the debtor has legal title, and the debtor only had equitable title to the real property in the trust. We stated that "[t]he trust remains valid; only the spendthrift clause is void, allowing creditors to reach the property held in trust by garnishment."[27] *Goff II* did not, as appellants argue, hold that creditors cannot reach the corpus of a self-funded trust with an invalid spendthrift clause. It held only that a judgment lien against the debtor did not create a secured claim against the assets of the trust. We have cited *Goff II* for the proposition that "[a] creditor can reach the trust assets" of a trust funded by the debtor-beneficiary.[28] As with the Bryant Family Trust, the trust in question (1) contained a spendthrift clause, (2) provided the debtor with a life interest in the income, with the remainder going to other beneficiaries, and (3) provided that the trustee could invade the corpus of the trust for the debtor's support, maintenance and welfare.

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bankruptcy estate because the federal ERISA statute is not "applicable nonbankruptcy law" under Bankruptcy Code § 541(c)(2) – was expressly overruled in *Patterson*, 504 U.S. at 757 n. 1, 112 S.Ct. at 2246 n. 1 (citing *Goff I*).

[27] *Goff II*, 812 F.2d at 933.

[28] *In re Latham*, 823 F.2d 108, 111 (5th Cir.1987).

Shurley points out that when she made the original contribution of the Marfa ranch to the trust, it was subject to a note and lien. She argues that this lien should affect our analysis, but we disagree. There is no dispute that Shurley was the owner of the ranch when she conveyed it to the trust, even if it was encumbered with a lien. The note and lien may have affected the value of the property at the time the trust was funded, but they did not affect ownership of the property. When determining the property of the estate, the Bankruptcy Code looks to the debtor's property "as of the commencement of the case."[29] It makes no more sense to look to the value of the ranch at the time of the creation of the trust than in [sic] does to look to the value of any other property of the debtor on the date of acquisition. If the debtor owns stock, bonds, real estate or other property, the original value or cost basis of those assets is irrelevant to the bankruptcy matter of defining the estate. Accordingly a lien on the ranch at the time of the trust's creation does not alter our conclusion that the ranch is property of the bankruptcy estate. The ranch might have appreciated or depreciated in value for any number of reasons since 1965, including the balance on the note, but it is still property of the bankruptcy estate.

Shurley argues that there was no proof by appellees that she had any equity in the ranch at the time of creation of the trust, reasoning that she could not be a self-settlor if the property she contributed was worthless. Assuming that Shurley is legally correct – that a settlor's contribution to a trust of real property in which she had

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[29] 11 U.S.C. § 541(a)(1).

no equity at the time of the trust's creation does not fall within the self-settlor rule – the bankruptcy court found that she had equity in the property at the time of the creation of the trust in 1965.[30] This fact finding is not clearly erroneous. Shurley purchased the ranch from her parents in 1950 for $131,366.64 and assumed a $50,000 balance on the note.[31] The balance on the note was only $23,000 when the property was conveyed to the trust.[32] Moreover, in the trust agreement itself, Shurley as a signatory represented that "the value of that portion of said real property to be contributed by [Shurley and her sister] each represents (1/6) of the total value of all of said real property to be contributed." This declaration is an admission by Shurley that the property she contributed had some value, exceeding the balance on the note, since the trust assumed the note.

B. *Beneficiary Control*

The bankruptcy court concluded that "[e]ither substantial control or self-settlement may operate to invalidate protective trust provisions."[33] It found that Shurley exercised too much control over the trust to qualify as the beneficiary of a spendthrift trust. We find none of the reasons given persuasive.[34]

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[30] *Shurley*, 171 B.R. at 778-79 n. 5.

[31] Shurley paid only $200 down for the ranch, and executed 25 separate promissory notes to her parents, which were annually forgiven by the parents.

[32] The note was subsequently paid off by the trust.

[33] *Shurley*, 171 B.R. at 782.

[34] We assume without deciding that the court was legally correct in concluding that "substantial control" can render a

First, the court found that "Mrs. Shurley, in conjunction with her father during his life, had the power to revoke, alter, or amend the Trust document, or distribute the Trust assets back to the settlors."[35] We disagree. The agreement provides that "M.D. Bryant (the father) with the concurrence of either Settlor Anne Bryant Ridge or Settlor Jane Bryant Shurley, shall have the right at any time during his lifetime to revoke, alter and amend said trust and distribute the assets of said trust to the Settlors in the same proportion as the original contributions by each of said Settlor, taking into account any adjustment under paragraph (b)." The power to revoke or amend the trust was vested in the father, not the daughters. Shurley had no authority to alter the trust. She only had the authority to prevent her father from doing so, and only if she and her sister vetoed the change. At most therefore she and her sister in combination had the power to ensure the perpetuation of the trust. Further, this power lapsed upon the death of the father in 1967. We find no authority that such a limited power rendered the trust subject of creditor claims against the beneficiaries.

Second, the bankruptcy court noted that the agreement provided that Shurley had the right to petition three "special trustees" for the partial or complete termination of the trust. The agreement provides for the appointment of certain named special trustees, including a state judge,

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spendthrift or other protective trust subject to creditor claims. We note however that we do not believe that appellees have cited any Texas authority for this proposition.

[35] *Id.* at 783.

after the death of the parents. It states that "[u]pon application made by either daughter . . . or both, showing that termination would best serve the intended purpose of the trust, such Special Trustees shall in their sole and absolute discretion have the power and authority by unanimous consent to terminate in whole or in part and from time to time the trust or trusts established hereunder." Again, this provision does not vest in Shurley the power to terminate or alter the trust. It only authorizes her to request such a change from special trustees, who have "in their sole and absolute discretion" the authority to alter the trust. Even absent such a provision, Shurley, like all Texas trust beneficiaries, had a statutory right to seek judicial modification or termination of the trust if "compliance with the terms of the trust would defeat or substantially impair the accomplishment of the purposes of the trust."[36] No court has ever held that such a statutory right renders a spendthrift trust subject to creditor claims.

Third, the bankruptcy court noted Shurley's special power of appointment. This provision merely gave the daughters the authority to allocate trust assets to their descendants. It grants no authority to the daughters to allocate assets to themselves. As explained above, the Bankruptcy Code expressly excludes such a power of appointment from the bankruptcy estate. Section 541(b)(1) of the Code provides that property of the estate does not include "any power that the debtor may exercise solely for the benefit of an entity other than the debtor."

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[36] Tex. Prop.Code Ann. § 112.054 (Vernon 1995).

Aside from the terms of the trust agreement, the bankruptcy court found that Shurley had exercised de facto control over the trust. The court found:

> Outside the Trust document, the Shurleys also manipulated Trust assets and governed the initial Trustee, Bryant Williams. The Shurleys were regularly able to obtain unrestricted corpus distributions and loans. While the Trust provides for such distributions, the liberality and circumstances under which they were requested and granted suggested a domination by M.D. Bryant, Mrs. Shurley and Mrs. Watkins of Mr. Williams. Only recently had any corpus distribution request been denied, and only recently had the successor Trustee, Mr. Armstrong, started to make only "loans," to the exclusion of corpus distributions. Indeed, in the early days of the Trust, the initial Trustee, on behalf of the Trust, executed promissory notes as a comaker for the Shurleys. Part of the malleability of Bryant Williams may have arisen either from his fear of being replaced for failing to abide by the wishes of Mrs. Shurley and Mrs. Watkins, or from his close relationship with the family. While M.D. Bryant, the Shurleys and the Watkines may not have held *all* of the puppet strings to Mr. Williams, they held enough of them to exert the control necessary to defeat the Trust's protective attributes.[37]

Shurley strongly denies that the evidence at trial supported these findings, arguing for example that there is no evidence that the first trustee ever made a single distribution of trust corpus or a single loan to Shurley or

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[37] *Shurley*, 171 B.R. at 783.

any other beneficiary. Appellees argue that in addition to the above-quoted findings, Shurley, among other things, "used the Trust income to induce extensions of credit to herself and her husband," and "engaged in 'trustee shopping' to help further her control of the trust assets."

Even if these findings are taken as undisputed, they do not establish control by the daughters over the trust assets sufficient to make the trust subject to their creditors. The fact that the trustees liberally bestowed trust assets on the daughters, by itself, does not establish de facto control by the daughters over the affairs of the estate. The daughters were after all two of the principal beneficiaries of the trust, and distributions of the wealth of the the trust to the daughters is entirely consistent with its apparent purpose. The agreement provides that the trustee was not limited to distributing income generated from the corpus of the trust. As discussed above, it expressly authorized the trustee to make distributions from the trust corpus "[i]f the trustee determines that the net income of said trust is insufficient to maintain and support any of the beneficiaries of said trust or their children and lineal descendants in their accustomed manner of living. . . . " It also expressly authorized the trustee to "loan money to . . . and otherwise deal with any and all persons" including "the beneficiaries of this trust."

As one Texas decision has explained in denying a creditor's claim against assets held by a spendthrift trust:

> the purpose of such a trust is not defeated by the fact that the trustee is authorized in his discretion to apply a part of the corpus of the fund to the use of the beneficiary in accordance

> with the terms of the trust. Neither is the purpose of such trust defeated by the fact that the trustee is authorized or even required to turn the entire trust fund or property over to the beneficiary absolutely at some fixed time in the future.[38]

Appellees did not establish that loans or grants from the trust to the daughters, on their face consistent with the purpose and language of the trust, amounted to de facto control of the trust by the daughters. Further, the fact that the beneficiary of a spendthrift trust may have behaved as a spendthrift only shows the prescience of the settlors, and should not defeat the protective features of the trust. Appellees' focus on the behavior of Shurley as beneficiary is misplaced, since as explained above, spendthrift trusts are not shielded from creditors "out of consideration for the beneficiary. Their justification is found in the right of the donor to control his bounty and secure its application according to his pleasure."[39]

C. *Whether the Trust Is an Annuity*

By separate appeal Shurley argues that the bankruptcy court erred in denying her summary judgment motion urging that her interest in the trust is an "annuity" exempt from creditors under Texas law.

Under Texas law and Bankruptcy Code § 522, Texas debtors may elect either state or federal exemptions from

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[38] *Adams v. Williams*, 112 Tex. 469, 248 S.W. 673, 679 (1923).

[39] *Hines v. Sands* 312 S.W.2d 275, 279 (Tex.Civ.App. – Fort Worth 1958, no writ).

creditors.[40] Shurley's claims that her interest in the trust is an annuity exempt from creditors under Tex. Ins. Code Ann. art. 21.22 (Vernon Supp.1997), which provides an exemption for "all money or benefits of any kind, including policy proceeds and cash values, to be paid or rendered to the insured or any beneficiary under any policy of insurance *or annuity contract* issued by a life, health or accident insurance company, including mutual and fraternal insurance, or under any plan or program of annuities and benefits in use by an employer *or individual.*" The emphasized language was added by a 1993 amendment to the statute, after Shurley filed for bankruptcy.

This argument fails for two reasons. First, her interest in the trust was not issued by an insurance company or employer, so the only conceivable claim of exemption is that her interest is part of a "plan or program of annuities and benefits in use by an . . . individual." The reference to an individual was added to the statute after the bankruptcy filing. In determining exemptions we must apply the law in effect at the time the debtor entered bankruptcy.[41] Although Texas exemption laws are liberally construed,[42] the exemption Shurley claims simply did not exist at the commencement of her bankruptcy case. We cannot agree with Shurley that the 1993 amendment merely "clarified" legislative intent insofar as it added a reference to non-employer annuities that are not issued

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[40] *In re Walden*, 12 F.3d 445, 448 (5th Cir.1994).

[41] *Walden*, 12 F.3d at 449 n. 7. In so holding, *Walden* was interpreting the same state statute at issue here, Insurance Code art. 21.22

[42] *Id.* at 448.

by insurance companies.[43] The statute plainly did not apply to such annuities prior to the amendment.

Second, we do not believe that Shurley's trust interest can be characterized as an annuity in any event. One Texas court has described an annuity as a "a form of investment which pays periodically during the life of the annuitant or during a term fixed by contract rather than on the occurrence of a future contingency."[44] We have cited this same definition with approval.[45] While all annuities do not make payments in fixed, predetermined amounts,[46] we do not believe that the term extends to a trust where future payments are highly contingent on the future circumstances of the beneficiaries. The trust agreement provides that the trustee "may" make distributions of trust corpus if he determines that such distributions

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[43] We assume without deciding that Shurley is correct that an annuity under the current statute can be issued by an entity other than an insurance company. *But see* art. 21.22(6) ("For purposes of regulation under this code, an annuity contract issued by a life, health, or accident insurance company, including a mutual company or fraternal company, or under any plan or program of annuities or benefits in use by an employer or individual, shall be considered a policy or contract on insurance."). Texas, like all states, comprehensively regulates insurers and insurance policies.

[44] *Steves & Sons, Inc. v. House of Doors, Inc.*, 749 S.W.2d 172, 175 (Tex.App. – San Antonio 1988, writ denied) (quoting *In re Howerton*, 21 B.R. 621 (Bankr.N.D.Tex.1982)).

[45] *In re Young*, 806 F.2d 1303, 1306 (5th Cir.1987) (quoting *Howerton*).

[46] With a variable annuity, "payments to the purchaser vary with investment performance." *NationsBank of North Carolina, N.A. v. Variable Annuity Life Ins. Co.*, 513 U.S. 251, 254, 115 S.Ct. 810, 812, 130 L.Ed.2d 740 (1995).

are needed to "maintain and support any of the beneficiaries or their children or lineal descendants in their accustomed manner of living." Any such good faith determination by the trustee is "final and binding on all interested parties." Such distributions were in fact made. By design, such distributions are tied to contingencies unknown at the time of the creation of the trust, and are not consistent with the concept that an annuity makes payments without regard to "the occurrence of a future contingency."[47] In addition, under terms of the trust agreement discussed above, payments to Shurley were contingent on (1) the death of her parents, since her interest increased on the death of one parent and increased again on the death of the second parent, (2) whether the father, with the consent of either sister, chose to terminate the trust, and (3) whether the special trustees terminated the trust.

Further, Shurley's argument simply proves too much, since if her interest in the trust is an annuity, then all beneficiaries of self-settled trusts could make the same argument, as long as the trust agreement called for periodic payments to the settlor for life or a fixed term. We cannot accept that the Texas legislature intended this result, which would reject the universally recognized rule, and one codified by Texas statute, that a settlor cannot create his own spendthrift trust and shield its assets from creditors. If the legislature had intended this result, it would have repealed Tex. Prop.Code Ann. § 112.035(d), which provides that "[i]f the settlor is also a

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[47] *Steves & Sons*, 749 S.W.2d at 175.

beneficiary of the trust, a provision restraining the voluntary or involuntary transfer of his beneficial interest does not prevent his creditors from satisfying claims from his interest in the trust estate."

CONCLUSION

In summary, we conclude that the Marfa ranch and income generated therefrom is property of the estate.[48] The judgment is reversed and the case is remanded for further proceedings consistent with this opinion.

REVERSED and REMANDED.

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[48] Income from the ranch belongs to the estate because the Bankruptcy Code defines property of the estate to include "[p]roceeds, product, offspring, rents, or profits of or from property of the estate." 11 U.S.C. § 541(a)(6).

APPENDIX 2

In re Billy R. SHURLEY and Jane Bryant Shurley, Debtors.

TEXAS COMMERCE BANK-SAN ANGELO, N.A., Texas Commerce Bank-Austin, N.A., and Dennis Elam, Chapter 7 Trustee, Plaintiffs,

v.

Billy R. SHURLEY and Jane Bryant Shurley and William H. Armstrong, II, Trustee, Defendants.

Bankruptcy No. 92-70484-RBK.
Adv. No. 93-7020-RBK.

United States Bankruptcy Court,
W.D. Texas,
Midland-Odessa Division.

Aug. 29, 1994.

Creditors and Chapter 7 trustee filed adversary proceeding against debtors and trustee of family trust. The Bankruptcy Court, Ronald B. King, J., held that: (1) debtor was settlor of discretionary spendthrift trust; (2) debtor's contribution to trust defeated trust's spendthrift and discretionary protection as to debtor's interest; (3) creditors could reach debtor's beneficial interest in trust, and were not limited to reaching debtor's initial contribution to trust corpus; (4) power of appointment granted to debtor in trust was special, and, thus, was excludable from estate property; and (5) injunction prohibiting distributions from trust was warranted.

Judgment accordingly.

John P. Higgins, Payne & Blanchard, L.L.P., Dallas, TX, for debtors Billy R. Shurley and Jane Bryant Shurley.

Michael G. Kelly, Odessa, TX, for Dennis Elam, Chapter 7 Trustee.

Eric J. Taube, Austin, TX, for Texas Commerce Bank-Austin, N.A.

Henry H. McCreight, Jr., Houston, TX, for Texas Commerce Bank-San Angelo, N.A.

AMENDED OPINION

RONALD B. KING, Bankruptcy Judge.

The question in this proceeding is whether the Debtor's interest as the beneficiary of a family trust is property of the Chapter 7 bankruptcy estate. This Court holds that the Debtor's interest in the trust is property of the estate because it does not qualify for spendthrift trust or discretionary trust protection under section 541(c)(2) of the Bankruptcy Code.[1]

I.

BACKGROUND

A. Parties.

The Plaintiffs in this adversary proceeding are two creditors, Texas Commerce Bank-Austin and Texas Commerce Bank-San Angelo (collectively "TCB"); and Dennis Elam, the Chapter 7 Trustee (Mr. Elam). The Defendants in this adversary proceeding are the Debtors, Billy R.

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[1] 11 U.S.C. § 541(c)(2) (1988). Title 11 is referred to herein as the Bankruptcy Code.

Shurley and Jane Bryant Shurley, and William H. Armstrong, II, the current Trustee of the M.D. Bryant Family Trust.

B. The Trust.

The M.D. Bryant Family Trust (the Trust) was created in 1965 by Trust Deed indicating that the settlors were M.D. Bryant, Ethel Bryant, Jane Bryant Shurley and Anne Bryant Ridge, now known as Anne Bryant Watkins.[2] M.D. and Ethel Bryant were the parents of Jane Bryant Shurley and Anne Bryant Watkins. Jane Bryant Shurley's contribution to the Trust res was a 10,947 acre tract of land (the Marfa Ranch) located in Presidio County, Texas and certain mineral interests located in Irion, Presidio, and Tom Green Counties, all located in Texas. The Trust instrument stated that Jane Bryant Shurley and Anne Bryant Watkins each contributed one-sixth of the total value of the Trust corpus, while the remaining two-thirds was contributed by M.D. and Ethel Bryant. These fractional contributions corresponded directly with the initial lifetime income interests enjoyed by the settlors.

On the death of M.D. and Ethel Bryant, Jane Bryant Shurley and Anne Bryant Watkins became equal, one-half lifetime income beneficiaries of the Trust. The Trust also granted each daughter a special power of appointment, executable by deed or will, over an adjusted one-half of

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[2] Jane Bryant Shurley and Anne Bryant Ridge were joined by their husbands in executing the Trust. Their joinder appeared to be merely pro forma, however. Neither Mr. Shurley nor Mr. Ridge were named as beneficiaries of the Trust.

the Trust assets. The special power of appointment allowed assignment of Trust assets only to lineal descendants, and prohibited appointment of Trust assets to Mrs. Shurley or Mrs. Watkins or their estates. The "adjusted one-half" referred to the Trustee's ability under the Trust instrument to equitably apportion Trust corpus, such that when Trust corpus was distributed to one beneficiary, that beneficiary's relative Trust interest would be decreased, or other beneficiaries would be provided similar corpus distributions.

The Trust contained both spendthrift and discretionary language. The spendthrift language prohibited voluntary or involuntary transfer of the beneficiary's interest in the Trust. The discretionary language allowed the Trustee almost complete discretion in his distribution of Trust income and corpus.

C. Positions of the Parties.

Plaintiffs contend that Mrs. Shurley's beneficial interest in the Trust is property of the bankruptcy estate pursuant to section 541(a). They argue that section 541(c)(2), which excepts "protective" trusts from property of the bankruptcy estate, does not apply because Mrs. Shurley's interest in the Trust does not qualify for either discretionary or spendthrift protection.[3] Plaintiffs allege

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[3] Spendthrift and discretionary trusts are referred to as "protective trusts" because they attempt to shield trust assets from creditors of beneficiaries. Some courts and authorities refer to all protective trusts generically as "spendthrift trusts" because they achieve similar goals of asset protection. It is helpful to keep the two kinds of trusts separate in analyzing the protective features.

that her interest in the Trust has lost, or was never entitled to, protection because (1) it was self-settled or (2) Mrs. Shurley exercised such control over the Trust and its assets so as to defeat the Trust's protective character. Plaintiffs further assert that Mrs. Shurley's special power of appointment over the adjusted one-half of the Trust assets is property of the bankruptcy estate, and that she should be enjoined from exercising the power of appointment. Finally, Plaintiffs argue that Mr. Armstrong should be enjoined from transferring Mrs. Shurley's interest in the Trust to anyone other than Mr. Elam.

Mrs. Shurley and Mr. Armstrong contend that Mrs. Shurley's beneficial interest in the Trust is not property of the estate because, pursuant to section 541(c)(2), the Trust's spendthrift and discretionary provisions protect Mrs. Shurley's interest in the Trust from the claims of creditors and the Bankruptcy Trustee. Mrs. Shurley also alleges that her interest in the Trust is protected as her inheritance under section 541(a)(5) and that her special power of appointment is not property of the estate under section 541(b)(1).

D. Bankruptcy Law.

Section 541(a)(1) defines property of the bankruptcy estate as "all legal or equitable interests of the debtor in property as of the commencement of the case." An inheritance, which the debtor "acquires or becomes entitled to acquire within 180 days" after filing a petition, also becomes property of the estate under section 541(a)(5). Thus, an inheritance accruing more than 180 days post-petition does not become property of the estate.

Section 541(c)(2) excepts from property of the estate the debtor's interest in a trust which contains "a restriction on the transfer of a beneficial interest of the debtor" which is enforceable under applicable nonbankruptcy law. Thus, if the Trust is entitled to protection as a spendthrift or discretionary trust under Texas law, the Bankruptcy Code allows enforceability of that protection. In addition, a power of appointment restricted to nondebtor beneficiaries is generally excluded from property of the estate pursuant to section 541(b)(1).

E. Issues.

1. To what extent, if any, is the beneficial interest of Jane Bryant Shurley property of the estate?
   a. Did the Trust create valid spendthrift or discretionary protection under Texas law?
   b. Is Jane Bryant Shurley a settlor of the Trust?
   c. To what extent, if any, does Jane Bryant Shurley's contribution to the Trust res defeat the Trust's spendthrift or discretionary protection as to her interest?
   d. Does Jane Bryant Shurley's beneficial interest qualify as an inheritance under section 541(a)(5)?
2. To what extent, if any, is the Special Power of Appointment property of the estate?
3. Is injunctive relief proper?

II.

DISCUSSION

A. The extent of Jane Bryant Shurley's beneficial interest as property of the bankruptcy estate.

1. Was the language sufficient to create a spendthrift or discretionary trust?

Texas courts have long recognized the validity of spendthrift protection for trust beneficiaries, at least where provisions prohibiting alienation are expressed. *Adams v. Williams*, 112 Tex. 469, 248 S.W. 673, 679 (1923); *Nunn v. Titche-Goettinger Co.*, 245 S.W. 421, 422 (Tex.Comm'n App.1922, judgmt. adopted); *First Bank & Trust v. Goss*, 533 S.W.2d 93, 95 (Tex.Civ.App. – Houston [1st Dist.] 1976, no writ). The Trust's anti-alienation provision was all encompassing and clearly intended to provide spendthrift protection:

> The interest of the beneficiaries in the trust estate and the increase and proceeds thereof, both legal and equitable, so long as the same are held in trust, shall not be subject in any manner to any indebtedness, judgment, judicial process, creditors' bills, attachment, garnishment, execution, receivership, charge, levy, seizures or encumbrance, of or against said beneficiaries; nor shall the interest of the beneficiaries in said trust be in any manner reduced or affected by any transfer, assignment, conveyance, sale, encumbrance, act, omission or mishap, voluntary or involuntary, anticipatory or otherwise, of said beneficiaries and said beneficiaries shall have no right or power to transfer, assign, convey, sell or encumber said trust estate and their

> interest therein, legal or equitable, during the existence of these trusts.

This language was sufficient to create spendthrift protection for the Trust.

Texas courts have also acknowledged the protection afforded beneficial interests by trust language granting the trustee discretion over trust asset distributions. *Hughes v. Jackson*, 125 Tex. 130, 81 S.W.2d 656, 659 (1935); *Kolpack v. Torres*, 829 S.W.2d 913, 915 (Tex.App. – Corpus Christi 1992, writ denied). The Trust gave the Trustee almost absolute discretion with regard to trust asset distributions. The Trust allowed the Trustee to either pay trust income to the life beneficiaries or allow the life beneficiaries to operate Trust ranch properties wholly or partially free of rent. In addition, the Trust allowed, but did not require, the Trustee to distribute "so much of the corpus of said trust as the trustee sees fit" to maintain the beneficiaries' "accustomed manner of living." This language equipped the Trustee with sufficient discretion to protect the beneficiaries' interest from the claims of creditors and make it a discretionary trust.

2. Was Mrs. Shurley a settlor?

A settlor is one who creates a trust, or furnishes consideration for the creation of a trust, though in form the trust is created by another. BLACK'S LAW DICTIONARY 1373 (6th ed. 1990) (citing RESTATEMENT (SECOND) OF TRUSTS § 3(1) (1959) and *Lehman v. Comm'r*, 109 F.2d 99, 100 (2d Cir.), *cert. denied*, 310 U.S. 637, 60 S.Ct. 1080, 84 L.Ed. 1406 (1940)); TEX.PROP.CODE ANN. § 111.004(14) (Vernon 1984) (" '[s]ettlor' means person who creates the trust"); *In re*

Brooks, 844 F.2d 258, 263 (5th Cir.1988) ("[t]he person who provides consideration for a trust is the settlor even if another person or entity nominally creates the trust"). By transferring property to the Trust, Jane Bryant Shurley created, at least in part, the Trust.[4] *City of Austin v. Cahill*, 99 Tex. 172, 189, 88 S.W. 542, 548, *reh'g denied*, 99 Tex. 201, 89 S.W. 552 (1905) ("[t]o constitute a direct trust, there must be a conveyance or transfer to a person capable of holding it; there must also be an object or fund transferred, and a cestui que trust or purpose to which the trust fund is to be applied."); *Kelly v. Lansford*, 572 S.W.2d 369, 373 (Tex.Civ.App. – Fort Worth 1978, writ ref'd n.r.e.) ("a person has a capacity to create a trust by transferring property inter vivos in trust"); IIA WILLIAM F. FRATCHER & AUSTIN W. SCOTT, SCOTT ON TRUSTS § 156.3 at 179-180 (4th ed. 1987) (hereinafter referred to as Scott on Trusts) ("Where the owner of property gratuitously transfers it in trust he is the settlor"); see TEX.PROP.CODE ANN. § 112.001 (Vernon 1984) ("A trust may be created by: . . . a property owner's inter vivos transfer of property to another person as trustee for the transferor or a third person."). The fact that co-creators contributed property to the Trust is of no consequence to Mrs. Shurley's status as a creator, nor is Mrs. Shurley's limited participation in the drafting

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[4] The Shurleys' argument that Mrs. Shurley *sold* the Marfa Ranch to the Trust is not supported by the facts. Mrs. Shurley never testified that she sold the Marfa Ranch to the Trust, or gave up her ownership rights in the Ranch solely in exchange for the Trust's assumption of the remaining balance on the Banker's Life note. Rather, she testified that she *conveyed* the property to the Trust because "it was a good deal" and "[w]e agreed that we would do what Daddy wanted."

of the Trust instrument relevant. Mrs. Shurley need only deliver property[5] (the Marfa Ranch and certain mineral

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[5] The Shurleys contend that Plaintiffs must prove that Mrs. Shurley had an *equity* interest in the Marfa Ranch at the time of its transfer to the Trust. If she did not have an equity interest they conclude that the transfer was not *gratuitous*, and, hence, Mrs. Shurley could not be a settlor. *See* SCOTT ON TRUSTS § 156.3 at 179-180 ("Where the owner of property gratuitously transfers in trust, he is the settlor."). This argument fails for several reasons. First, the definition of settlor only requires a transfer of a *property* interest; the debtor need not have equity to have a property interest. Here, Mrs. Shurley had fee simple ownership of the Marfa Ranch subject to a deed of trust securing a note, which had a remaining balance of roughly $24,000. Mrs. Shurley transferred that property interest to the Trust. Second, even if an equity interest was required, it is apparent from the facts that Mrs. Shurley had such an interest. It is highly improbable that a 11,000 acre ranch in Presidio County, Texas that "sold" for $131,366 in 1950 would have subsequently decreased in value to less than $24,000 in 1965 (18% of its original value). Indeed, the estate tax return of M.D. Bryant shows the value per acre of the "other half" of the Marfa Ranch in 1967 was approximately $17.50. The Shurleys' argument would place the value of Mrs. Shurley's "half" of the Ranch at just over $2 per acre in 1965, a value that is hard to accept in light of the 1967 $17.50 per acre figure.

Third, while it is true a gratuitous property transfer clearly establishes a settlor, this does not necessarily mean that a non-gratuitous transferor is not a settlor. Indeed, the current statute, like the prior law, does not clearly distinguish between gratuitous and non-gratuitous property transfers. *Kelly*, 572 S.W.2d at 373 ("a person has a capacity to create a trust by transferring property inter vivos in trust"); TEX.PROP.CODE ANN. § 112.001 (Vernon 1984) ("A trust may be created by: . . . a property owner's inter vivos transfer of property to another person as trustee for the transferor or a third person . . . "). Fourth, Mrs. Shurley's counsel admitted Mrs. Shurley "had an equity interest, if you use 1950 values, of about $26,000 of that property at the time she put it into the [trust] estate."

interests) in trust to some trustee for the benefit of some beneficiaries (Jane Bryant Shurley, Anne Bryant Watkins, M.D. Bryant, Ethel Bryant and all of their lineal descendants). *Cahill*, 99 Tex. at 189, 88 S.W. at 548.

Moreover, even if Mrs. Shurley's limited participation in the creation of the Trust instrument served to take away her "creator" status, Mrs. Shurley became a settlor by furnishing consideration for the creation of a trust. *Brooks*, 844 F.2d at 263; *Lehman*, 109 F.2d at 100; SCOTT ON TRUSTS § 156.3 at 179-80. The consideration was the Marfa Ranch and certain mineral interests. In effect, Mrs. Shurley exchanged her property interest in the Marfa Ranch and the mineral interests for a beneficial interest in the Trust.

The Trust specifically referred to Mrs. Shurley as a settlor. A subsequent "Memorandum of Trust Agreement" stated that Mrs. Shurley, along with the Bryants and Mrs. Watkins, had "created" the Trust. Unambiguous language in a trust makes it unnecessary to use extrinsic evidence to construe the instrument. *Corpus Christi Bank & Trust v. Roberts*, 587 S.W.2d 173, 187 (Tex.Civ.App. – Corpus Christi 1979), *aff'd*, 597 S.W.2d 752 (Tex.1980). The parol evidence rule applies to trust documents. *City of Mesquite v. Malouf*, 553 S.W.2d 639, 643 (Tex.Civ.App. – Texarkana 1977, writ ref'd n.r.e.). Absent fraud, accident or mistake, parol evidence is inadmissible to contradict or vary the terms of an unambiguous agreement. *Jackson v. Hernandez*, 155 Tex. 249, 260, 285 S.W.2d 184, 190 (1955). The Trust unambiguously named Jane Bryant Shurley as a settlor. Even if credible evidence to the contrary had been offered, which it was not, this Court may properly disregard such evidence.

Finally, Mrs. Shurley signed the Trust and the Memorandum of Trust Agreement. Typically, only settlors sign trust instruments because they are the only parties intended to be bound. Beneficiaries rarely sign a trust instrument because their signature is irrelevant: they have neither placed property in trust, nor given consideration for creation of the trust. Notably, in this case, other contingent beneficiaries existed at the time the Trust and Memorandum of Trust Agreement were executed, but they did not sign either document, and a guardian ad litem did not sign in their stead. Clearly, Mrs. Shurley was a settlor of the Trust.

3. To what extent, if any, does Jane Bryant Shurley's contribution to the Trust res defeat the Trust's spendthrift or discretionary protection as to her interest?

Mrs. Shurley's contribution to the Trust defeats the Trust's spendthrift and discretionary protection as to her interest. To understand why this is so requires an examination of (1) the policy behind self-settled trust rules, (2) the distinction between spendthrift and discretionary trust at tributes, and (3) the case law regarding self-settled spendthrift and discretionary trusts.

a. Protective trust policy.

Two foundation policies support the validity of protective trusts. First, the law generally attempts to uphold the intention of a testator or donor. Since a testator or donor could condition a bequest or gift during the life of the beneficiary or donee, a similar policy should apply to

a settlor. Second, spendthrift trust provisions are upheld under the rationale that a beneficiary's creditor has no right to rely on the assets and income of a protective trust. Creditors not diligently investigating the availability of trust assets should not be able to later complain about a spendthrift or discretionary provision that existed at trust creation. Similarly, the foundation policy advocating the *in* validity of *self-settled,* protective trusts contends that "[i]t is against public policy to permit a man to tie up his own property in such a way that he can still enjoy it but can prevent his creditors from reaching it." SCOTT ON TRUSTS § 156 at 167; *Glass v. Carpenter,* 330 S.W.2d 530, 533-34 (Tex.Civ.App. – San Antonio 1959, writ ref'd n.r.e.). This corresponds to the old adage that "you can't have your cake and eat it too." These opposing policies turn primarily on one factor – control. Where a settlor has relinquished control over his assets, he ought to be able to condition the transfer and his creditors cannot complain about the conditions. On the other hand, protective trust self-settling is a form of control that unfairly handicaps present and future creditors without restricting a settlor's beneficial use of the assets.

b. Distinguishing spendthrift and discretionary trusts.

"Spendthrift" and "discretionary" provisions in a trust shield trust assets from creditors of trust beneficiaries. Trusts with language prohibiting the voluntary or involuntary alienation of the beneficial interest in the trust are considered "spendthrift trusts." Spendthrift

trusts provide *direct* protection from creditors of a beneficiary by expressly forbidding alienation of the beneficiary's interest in the trust. RESTATEMENT (SECOND) OF TRUSTS § 152 (1959); SCOTT ON TRUSTS § 152; GEORGE G. BOGERT & GEORGE T. BOGERT, THE LAW OF TRUSTS AND TRUSTEES § 222 (2d ed. rev. 1992) (hereinafter referred to as BOGERT ON TRUSTS). On the other hand, trusts granting a trustee uncontrolled discretion to distribute or not distribute trust income or corpus are considered "discretionary trusts."[6] Discretionary trusts provide *indirect* protection from creditor attachment by placing responsibility for alienation of trust assets with the trustee. RESTATEMENT (SECOND) OF TRUSTS § 155 cmt. b. (1959); SCOTT ON TRUSTS § 155; BOGERT ON TRUST § 228. Generally, courts prevent creditors of a beneficiary from attaching trust assets if the trustee controls the time, amount, and manner of payments to a beneficiary. A trust simultaneously possessing both spendthrift *and* discretionary attributes is labeled a discretionary spendthrift trust. *See, e.g., Altman v. Comm'r*, 83 B.R. 35 (D.Haw.1988); *Wilson v. United States* (*In re Wilson*), 140 B.R. 400, 404-06 (Bankr.N.D.Tex.1992).

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[6] The term "discretionary trust" is a term of art most often seen in opposition to the terms "support trust" or "right-to-receive trust." These three trust attributes cover the spectrum of trustee discretion with respect to distribution of trust corpus and income. In a "right-to-receive trust," a beneficiary has a vested right to receive an ascertainable portion of the trust income or principal – the trustee has no discretion. In a "support trust," the beneficiary has right to receive so much of the trust income or principal as is necessary for his education or support – the trustee has limited discretion. In a discretionary trust, the beneficiary has no right to receive trust income or principal – the trustee has sole and absolute discretion.

c. Case law.

1. Protective trust self-settling.

Discretionary and spendthrift provisions provide two layers of protection: direct (spendthrift) and indirect (discretionary) restraints on trust asset alienation. SCOTT ON TRUSTS, § 156. In a discretionary spendthrift trust, the threshold question is whether creditors can defeat the spendthrift and discretionary provisions in the trust. *See Fewell v. Republic Nat'l Bank of Dallas*, 513 S.W.2d 596, 599 (Tex.Civ.App. – Eastland 1974, writ ref'd n.r.e.) (spendthrift provisions of trust are severable and, when defeated, do not destroy the whole trust agreement). Texas courts have consistently upheld the spendthrift shield in the face of creditor attack on a beneficial trust interest. *Adams v. Williams*, 112 Tex. 469, 248 S.W. 673 (1923); *see* BOGERT ON TRUSTS § 222 n. 59. Most cases hold otherwise, however, where a settlor creates a trust in which he is also a beneficiary – a self-settled trust. *Glass*, 330 S.W.2d at 533; *see* TEX.PROP.CODE ANN. § 112.035(d) (Vernon 1984).[7] Because Mrs. Shurley was a settlor, the spendthrift provision in her favor is not effective.[8]

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[7] TEX.PROP.CODE ANN. § 112.035(d) (Vernon 1984) provides:

> If the settlor is also a beneficiary of the trust, a provision restraining the voluntary or involuntary transfer of his beneficial interest does not prevent his creditors from satisfying claims from his interest in the trust estate.

Although this provision did not exist at the time of Trust creation in 1965, the statute accurately codifies trust law existing prior to 1984 in Texas. *See* BOGERT ON TRUSTS § 223 n. 59.

[8] The Shurleys' reliance on *Hines v. Sands*, 312 S.W.2d 275 (Tex.Civ.App. – Fort Worth 1958, no writ), is misplaced. In *Hines*,

Texas courts have also found discretionary trusts nearly impregnable to creditor attack. *Hughes v. Jackson*, 125 Tex. 130, 136-37, 81 S.W.2d 656, 659 (1935); *Kolpack v. Torres*, 829 S.W.2d 913, 915 (Tex.App. – Corpus Christi 1992, writ denied). Self-settling, however, can defeat the protective nature of discretionary trust provisions. It does not matter whether spendthrift provisions, discretionary provisions, or both are found in the trust instrument; the self-settled trust loses the asset shield provided by both to the extent of the trustee's discretion. *Bank of Dallas v. Republic Nat'l Bank of Dallas*, 540 S.W.2d 499, 500-02 (Tex.Civ.App. – Waco 1976, writ ref'd n.r.e.) (discretionary spendthrift trust defeated by self-settling); *Glass*, 330 S.W.2d at 533 ("one cannot settle upon himself a spendthrift or other protective trust, or purchase such a trust from another, which will be effective to protect either the income or corpus against the claims of his creditors, or to free it from his own power of alienation") (emphasis added); RESTATEMENT (SECOND) OF TRUSTS §§ 156(1) & 156(2) (1959); ERWIN N. GRISWOLD, SPENDTHRIFT TRUSTS § 481 (2d

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a creditor sought to garnish the beneficial interest of an employee in an employer's spendthrift, profit-sharing trust. The *employee contributed nothing* to the trust. The employer contributed a portion of businesses' net profits to the trust and then, at its discretion, distributed profit bonuses to the employees. The court specifically found that the employee was not a settlor, despite the argument that the employee gave consideration (skilled labor) for the trust creation. *Id.* at 278. *Hines* is thus not a self-settled trust case. Moreover, the employee beneficiary in *Hines* had no control over potential distributions. Here, Mrs. Shurley self-settled a discretionary spendthrift trust and had some control over potential distributions (e.g., a special power of appointment).

ed. 1947);[9] SCOTT ON TRUSTS, § 156.2; BOGERT ON TRUSTS § 228. The existence of other possible beneficiaries makes no difference. *See Altman v. Comm'r*, 83 B.R. 35, 37 (D.Haw.1988) (citing *Cooke Trust Co. v. Lord*, 41 Haw. 198, 205 (1955)) (the entire trust corpus could be reached by the settlor's creditors, despite the existence of other possible beneficiaries, where the terms of the trust allowed the trustee to pay all trust income to the settlor-beneficiary). Moreover, the self-settling rule applies irrespective of fraudulent intent.[10] *Glass*, 330 S.W.2d at 533; RESTATEMENT

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[9] § 481 DISCRETIONARY TRUSTS. The settlor may attempt to retain a beneficial interest free from the claims of his creditors, by giving his property to a trustee and investing the trustee with complete discretion to decide whether the income shall be paid to him and, if so, how much of it. Thus, A may convey property to T on trust to pay to A during A's life so much of the income as in T's uncontrolled discretion he deems wise, with a provision that on A's death the principal and any accumulated income shall be conveyed to B. The remainder, so far as the principal is concerned, being a present vested remainder in B and not subject to A's control, is beyond the reach of A's creditors, unless the transfer is a fraudulent conveyance. Does the fact that the trustee is given discretion over the disposition of the income exempt the income, likewise, from the claims of creditors? The courts have very properly held that in such a case creditors of the settlor may reach the entire income from the trust property during his life [FN omitted]. A person can not settle his own property so that it will be free from the claims of creditors and yet retain the right to receive the income, if it is paid to any one, during his lifetime.

[10] The Shurleys confuse protective trust with fraudulent conveyance policy when they argue that creditors should not get any more than they would have received "if [Mrs. Shurley] had not purported to tie up her assets." Protective trust policy against self-settling does not require actual or constructive fraud on creditors; it is enough that a settlor has retained

(SECOND) TRUSTS § 156, cmt. a (1959). Because Mrs. Shurley was a settlor, the discretionary provision does not shield her interest in the Trust.

2. Dominion and control of settlor.

To place any of Mrs. Shurley's beneficial interest into the bankruptcy estate, the Shurleys argue that Plaintiffs must show two elements: (1) self-settling and (2) control by the settlor. This is incorrect. No Texas case has required anything other than self-settling to defeat a protective trust. *Daniels v. Pecan Valley Ranch, Inc.*, 831 S.W.2d 372, 378 (Tex.App. – San Antonio 1992, writ denied), *cert. denied*, 113 S.Ct. 2944, 124 L.Ed.2d 692 (1993); *Bank of Dallas*, 540 S.W.2d at 501; *Glass*, 330 S.W.2d at 533-34; *see* TEX.PROP.CODE ANN. § 112.035 (Vernon 1984). Nor does the relevant section of the RESTATEMENT, adopted by Texas and federal courts, require control in addition to self-settling. RESTATEMENT (SECOND) OF TRUSTS § 156 (1959); *Bank of Dallas*, 540 S.W.2d at 501; *Brooks*, 844 F.2d at 261. The pension trust cases on which the Shurleys rely do not

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beneficial use, without the possible burden of creditor attachment. RESTATEMENT (SECOND) OF TRUSTS § 156, cmt. a (1959). Some debtors transfer or conceal assets with the intent to defraud or elude *contemporaneous* creditors; creditors attempting to avoid these fraudulent conveyances are generally limited in their recovery to the debtor's assets *prior* to transfer. No one has alleged Mrs. Shurley created the Trust to defraud 1965 creditors. In 1965, had the creditors asserted claims to trust assets *under a fraudulent conveyance* theory, they might have extracted Mrs. Shurley's initial contribution from the Trust. Had they asserted the self-settled trust rule, they would have recovered the "interest" Mrs. Shurley "received" or retained under the Trust.

require control *in addition* to self-settling to defeat protective provisions.

Federal courts in the Fifth Circuit have examined the validity of "spendthrift" protection in the pension and Employee Retirement Income Security Act (ERISA) trust context through the looking glass of both beneficiary control *and* self-settlement. *Brooks*, 844 F.2d at 263-64; *In re Goff*, 706 F.2d 574, 588 (5th Cir.1983); *In re Kirk*, 101 B.R. 476, 478 (Bankr.N.D.Tex.1989). Either substantial control *or* self-settlement may operate to invalidate protective trust provisions. Like self-settling, beneficiary control of trust assets is contrary to protective trust rules in that it allows the beneficiary to access what creditors are forbidden. *Goff*, 706 F.2d at 588; RESTATEMENT (SECOND) OF TRUSTS § 153(2) (1959) ("[i]f the beneficiary is entitled to have the principal conveyed to him immediately, a restraint on the voluntary or involuntary transfer of his interest in the principal is invalid."); RESTATEMENT (SECOND) OF TRUSTS § 341, cmt. c (1959) (invalidating spendthrift trust provisions where the sole beneficiary is also the sole trustee). The greater the contributions and the more control an employee has over the contributions to and distributions from a pension trust, the less likely it is the court will enforce protective provisions in a trust, and the more likely it is the employee will be labeled a "settlor." *Brooks*, 844 F.2d at 263-264; *Kirk*, 101 B.R. at 478; *see In re James*, 126 B.R. 360, 362 (Bankr.D.Kan.1991) (where only the employer contributed to pension plan and where the employee-beneficiary had only limited control over trust assets, the 401(k) plan was not self-settled, despite loan and early distribution provisions). Some courts find control, particularly by an alter ego organization, a sufficient

condition in and of itself to deny the validity of protective provisions. *In re Kaplan*, 97 B.R. 572 (9th Cir. BAP 1989). Although the Shurleys claim that these ERISA cases support the proposition that dominion and control are required, in addition to self settlement, Texas spendthrift law does not require any more settlor control than is evidenced by self-settling.

Even if Texas law did require control in addition to self-settling, however, Mrs. Shurley exhibited sufficient dominion and control over the Trust assets to defeat the Trust's protective character. Mrs. Shurley had extensive control under the Trust instrument itself. First, Mrs. Shurley, in conjunction with her father during his life, had the power to revoke, alter, or amend the Trust document, or distribute the Trust assets back to the settlors. Second, from and after two years following the death of Ethel Bryant, Mrs. Shurley and Mrs. Watkins had the right to petition three "special trustees" for the partial or complete termination of the Trust. The special trustees then had the power to terminate the Trust, with the Trust assets passing equally to Mrs. Shurley and Mrs. Watkins. With no trust res, the special trustees would appear to have no fiduciary duties and would likely "rubber stamp" a decision by Mrs. Shurley and Mrs. Watkins to terminate the Trust. Third, Mrs. Shurley retained and received a special power of appointment over half the Trust assets. The power was exercisable inter vivos or by will. While a special power of appointment, by itself, would not invalidate a protective trust, it is an indication of control when it is retained by a settlor.

Outside the Trust document, the Shurleys also manipulated Trust assets and governed the initial Trustee, Bryant Williams. The Shurleys were regularly able to

obtain unrestricted corpus distributions and loans. While the Trust provides for such distributions, the liberality and circumstances under which they were requested and granted suggested a domination by M.D. Bryant, Mrs. Shurley and Mrs. Watkins of Mr. Williams. Only recently had any corpus distribution request been denied, and only recently had the successor Trustee, Mr. Armstrong, started to make only "loans," to the exclusion of corpus distributions. Indeed, in the early days of the Trust, the initial Trustee, on behalf of the Trust, executed promissory notes as a comaker for the Shurleys. Part of the malleability of Bryant Williams may have arisen either from his fear of being replaced for failing to abide by the wishes of Mrs. Shurley and Mrs. Watkins, or from his close relationship with the family. While M.D. Bryant, the Shurleys and the Watkinses may not have held *all* of the puppet strings to Mr. Williams, they held enough of them to exert the control necessary to defeat the Trust's protective attributes.

Furthermore, the Shurleys held out Trust assets to creditors as if they controlled the assets. In letters and in financial statements, the Shurleys repeatedly treated the Trust as just another bank account from which they could withdraw funds at will. While Generally Accepted Accounting Principles (GAAP) require the reporting of a beneficial interest in a trust on a personal financial statement, the interest must be explained to indicate its nature and extent. The Shurleys suggest that any explanation would require a legal opinion, which GAAP prohibits. An explanation need not, however, include a legal opinion, but rather only a factual explanation. In one instance, the Shurleys reported *all* of the Trust assets (approximately five million dollars in value) in their financial statement

submitted to the bank, when in fact Mrs. Shurley had only beneficial rights in one-half of the Trust. Certainly, it was incumbent upon the creditors relying upon the financial statements to perform a sufficient due diligence inquiry into the nature of the Trust. The issue in this adversary proceeding is not whether there were creditor mistakes, however, but whether the Shurleys controlled and manipulated Trust assets to their benefit.[11] The Shurleys' reporting of the Trust corpus as an asset on their balance sheet in order to obtain credit exhibited their perception of control over the Trust assets. On the whole, Mrs. Shurley held and exercised sufficient control to defeat the protective character of the Trust.

3. Extent of creditor's reach.

The more difficult question requires a determination of the *extent* of the creditor's reach into a self-settled, discretionary spendthrift trust. The Shurleys argue that the reach should be limited to Mrs. Shurley's initial contribution to the Trust corpus, because that is all that would have been available for the creditors in the first place.[12] They argue that Mrs. Shurley's "interest" in the

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[11] Because a separate adversary proceeding concerning dischargeability of debt is pending, no findings are made concerning reasonable reliance by TCB or intent to deceive by the Shurleys.

[12] The Shurleys' argument is appealing at first blush: it limits creditors to what Mrs. Shurley had before entering into the Trust agreement and gives the residue to the other, innocent beneficiaries, Mrs. Shurley's children, M.D. Bryant's grandchildren. The Shurleys' argument, however, has several fatal flaws: it ignores future creditors and requires intricate

Trust is limited to her initial contribution to the Trust assets. *See* RESTATEMENT (SECOND) TRUSTS § 156(1) (1959). Plaintiffs argue that the reach extends to the maximum amount of the Trust that could be applied for her benefit. *Bank of Dallas*, 540 S.W.2d at 499; RESTATEMENT (SECOND) TRUSTS § 156(2) (1959).

Self-settling of a *spendthrift* trust defeats the non-alienability of the trust to the extent of the settlor-beneficiary's "interest." RESTATEMENT (SECOND) TRUSTS § 156(1)

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tracing and valuation of antique assets. The argument concentrates on the 1965 Trust creation, accounting for only those creditors that were present at the Trust creation and ignoring subsequent creditor reliance on Mrs. Shurley's interest in a changing asset mix. In 1965, Mrs. Shurley's creditors knew the extent of Mrs. Shurley's property and presumably should not be entitled to anything more than that property. Had those creditors attacked the spendthrift character of the Trust in 1965, they would have been limited to Mrs. Shurley's "interest" in the Trust (at that time Mrs. Shurley was entitled only to 1/6 of the Trust income, the presumed equivalent of her contribution to the Trust res). The same limits cannot be applied to Mrs. Shurley's subsequent creditors.

Subsequent creditors had a different reliance interest at stake. In 1971, after the deaths of M.D. and Ethel Bryant, the extent of Mrs. Shurley's interest in the Trust changed dramatically; she acquired a discretionary, one-half income and corpus interest in the Trust. With the knowledge of this beneficial interest, subsequent creditors looked beyond Mrs. Shurley's initial contribution for satisfaction of their claims. If the spendthrift character of the Trust was invalid from the beginning, then Mrs. Shurley would have been unable to shield subsequent assets placed in the Trust or directly inherited. For example, had the M.D. Bryant Trust never been created, Mrs. Shurley presumably would have inherited one-half of her parents' estate, which would be subject to creditor attachment. The fact that this "inheritance" is in Trust does not change what creditors can reach absent valid spendthrift or discretionary protection.

(1959). Self-settling of a *discretionary* trust defeats the non-alienability of the trust to the "maximum amount which the trustee under the terms of the trust could pay to [the settlor-beneficiary] or apply for his benefit." RESTATEMENT (SECOND) TRUSTS § 156(2) (1959). This raises two questions: (1) to what extent does self-settling of a *discretionary spendthrift trust* defeat the non-alienability of the trust assets; and (2) what is the difference between the settlor-beneficiary's "interest" and "the maximum amount which the trustee under the terms of the trust could pay . . . or apply for his benefit?"

There is no difference between a settlor-beneficiary's "interest" and "the maximum amount" in the context of a discretionary spendthrift trust. The RESTATEMENT language in sections 156(1) and (2) addresses different concerns. When a *spendthrift* provision is defeated via self-settling, the law is concerned with establishing the settlor-beneficiary's current "interest" in the trust, not the extent of the trustee's discretion. When a *discretionary* provision is defeated via self-settling, the law is concerned with establishing the extent of the trustee's discretion, so as to determine what the trustee can withhold from attaching creditors.[13]

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[13] For example, the interest of a sole settlor retaining a 1/10 beneficial interest in a trust is reachable under discretionary trust law only to the extent of his 1/10 interest, the extent of his retained control (the settlor might otherwise have just given away the remaining 9/10 interest, in which case the creditors would not recover anything). The interest of a settlor who contributes 1/10 of the assets to a discretionary trust and becomes the sole beneficiary, however, is completely subject to the claims of creditors, again, the extent of his retained control.

If a trust provided one of two beneficiaries with a one-half corpus and income interest in a trust, then, absent spendthrift and

In other words, whether spendthrift protection exists is a threshold question possibly subjecting the settlor-beneficiary's "interest" to liability, but the *extent* of that "interest" is determined by the breadth of the trustee's discretion. The extent of the trustee's discretion is irrelevant to the validity of the spendthrift protection; either the spendthrift attribute exists, or it does not. If it does not, then creditors can reach whatever present or future "interest" the settlor-beneficiary retains. Once the spendthrift provision is defeated, however, the secondary inquiry concerns the extent of the beneficial interest that the trustee *could* distribute to the beneficiary under the discretionary terms of the trust. This prospective inquiry determines the extent to which creditors can reach trust assets.

The extent of a creditor's reach in a self-settled trust should not depend upon a settlor's initial contribution.[14]

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other discretionary language, the creditors of one of the beneficiaries could only reach one-half of the trust assets, the beneficiary's "interest." If a spendthrift provision was added, the creditors could not reach any trust assets, except, perhaps, under a fraudulent conveyance theory. If one of the beneficiaries was also the sole settlor of the spendthrift trust, however, creditors could reach that settlor-beneficiary's "interest," one half of the trust assets. If discretionary language were added to the trust, allowing the trustee to reach only one-half of the trust *income*, not corpus, for the benefit of the settlor-beneficiary, the creditors are further limited to one-half of the trust income, "the maximum amount" the trustee could pay or apply for the benefit of the settlor. Thus, the "interest" and "maximum amount" provisions coexist; the first addresses the primary, spendthrift inquiry, while the second addresses the discretionary inquiry.

[14] The Shurleys' argument to the contrary is based on distinguishable or insupportable case law. One case, *State v. Nashville Trust Co.*, 28 Tenn.App. 388, 393-95, 190 S.W.2d 785,

Only a beneficiary, not a settlor, has an "interest" in the trust. A settlor "contributes" or "delivers" property to the

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787-88 (1945), follows the RESTATEMENT rule: "If the beneficiary of a spendthrift trust *already created* pays off encumbrances on the trust property, the beneficiary *has to that extent created a spendthrift trust for himself* and his creditors can reach *his interest to the extent of his payment.*" RESTATEMENT (SECOND) OF TRUSTS § 156, cmt. f (1959) (emphasis added). This apparent exception to the self-settled trust rule carves out a self-settled trust within a spendthrift trust "already created" for the special purpose of preventing a debtor from converting unprotected assets to protected assets. In this context, the rule prevents a debtor from shielding otherwise unprotected assets merely by paying down the debt on protected assets. Mrs. Shurley's case is distinguishable in that she was one of the initial creators of the Trust, not someone seeking to put unprotected assets into an otherwise valid spendthrift trust. She bargained for, and received, an interest in the Trust in exchange for her contribution of the Marfa Ranch. She did not merely pay down an encumbrance to convert unprotected assets, thereby becoming a special purpose "settlor."

In *McKeon v. Department of Mental Health* (*In re Johannes Trust*), 191 Mich.App. 514, 529, 479 N.W.2d 25, 29 (1991), the court concluded, in a cursory fashion and without offering any support, that creditors of a partially self-settled discretionary trust, which was created for a mentally disabled person, could only reach "that portion of the [trust] assets that came from the [self-settlor]." The RESTATEMENT (SECOND) OF TRUSTS § 156 is not so limited, nor is Texas law.

The Shurleys also mistakenly rely on a footnote in *Farmers State Bank v. Janish*, 410 N.W.2d 188 (S.D.1987). In that case, a judgment creditor sought to garnish a debtor's interest in a spendthrift trust. The Shurleys cite the following footnote for support: "*Although not significant* here because [the debtor's] share in the trust is sufficient to satisfy the creditor's claim, it should be noted that only the *interest* of the debtor in the trust can be reached by her creditors." *Id.* at 190 n. 2 (emphasis added). First, this is dicta, not a holding. Second, the quotation

trust, but has no "interest" other than what he retains *as a beneficiary*. The Iowa Supreme Court best expressed this principle in addressing the contention that creditors of a defeated spendthrift trust should be limited to the initial contribution of the self-settlor:

> That the settlement, the abandonment of the [will] contest, and the surrender of the lots devised to [the self-settlor] constitute consideration is hornbook law, but it is insisted that though this be so, it does not subject the trust property, that it merely makes the trust enforceable, and that, therefore all that can in any event be subjected is the consideration paid. We are not impressed with the argument. *When a debtor purchases property, what he pays for it is gone from his creditor.* That alone is sufficient reason why such consideration should not be subjected to the debt. *By the same token, the property bought is the fund the creditor may resort to.* He cannot complain that the debtor did not get enough. He has the right to avail himself of the profits if the debtor did not pay enough.

De Rousse v. Williams, 181 Iowa 379, 164 N.W. 896, 899 (1917) (emphasis added). Here, the situation is similar. Mrs. Shurley traded the Marfa Ranch for a beneficial

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does not indicate that "creditors could reach only the debtor's contributions to a trust, not the contributions of other settlors," as the Shurleys represent in their brief. Rather, the quotation restates the rule announced in RESTATEMENT (SECOND) OF TRUSTS § 156(1) (1959) that creditors can only reach a self-settlor's "interest" in a spendthrift trust. As discussed *infra*, a self-settlor's "interest" is unrelated to a self-settlor's "contribution." If Janish intended to limit the extent of the creditors' reach to only the settlor's contributions, this Court disagrees.

interest in the Trust. As such, the creditors can only reach what Mrs. Shurley "bought," not what she "paid." Despite the Trustee's decision to retain the Ranch, the Ranch is no longer "available" to the creditors under a self-settled trust theory.[15] Had the Trust exchanged the Ranch for an asset that yielded a 500% return, the creditors would get a windfall; had the Trust exchanged the Ranch for a peppercorn, the creditors would suffer a loss. Either way, the creditors can reach the maximum amount which the Trustee could distribute for Mrs. Shurley's benefit – Mrs. Shurley's beneficial interest in the Trust.[16]

In addition, the fact that a settlor's initial contribution *remains in the trust* should not be relevant to what creditors can reach. The Marfa Ranch's continuation as a Trust asset should not limit the creditors' recovery. The rule forbidding self-settling must not vary merely because the initial contribution is easily traceable. Had the Marfa Ranch been sold years ago, the court could face a near impossible burden of having to value a decades or

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[15] A fraudulent conveyance theory may have allowed creditors to reach the Marfa Ranch had creditor action been contemporaneous with trust creation. However, under self-settled trust doctrine, future creditors are only entitled to rely on the "interest" of the beneficiary, be it fertile or barren.

[16] The court does not reach the question of whether the circumstances surrounding trust creation constituted an "integral plan" by the Bryants, Mrs. Shurley and Mrs. Watkins, so as to possibly subject the trust to the "reciprocal trust" doctrine, rendering all participants settlors in the entirety of the Trust assets.

The court also finds it unnecessary to decide whether a trust can be revocable for tax purposes and still retain its spendthrift and discretionary protection.

century old trust contribution. Such a value would be of precarious validity. Future creditors should not have to trace the proceeds of trust assets "turned-over" numerous times after trust creation to meet their burden of proof. Courts should not have to value property placed in trust decades before, where the evidence of such value is non-existent or was created by the settlor himself to obtain a lower property tax valuation. Allowing recovery only to the extent of the settlor's initial contribution could lead to inconsistent results, depending on whether assets were retained or sold, and if retained, whether their value went up or down. The Shurleys' argument is not persuasive.

d. Beneficial interest as inheritance.

The Shurleys' attempt to characterize Mrs. Shurley's Trust interest as "inheritance" for purposes of section 541(a)(5) fails. The Trust is an inter vivos trust created in 1965. M.D. Bryant died in 1967, and Ethel Bryant died in 1971. While it is true that pour over provisions in the Bryants' wills left the bulk of their estates to the Trust, this does not alter the fact that the Trust was created inter vivos. Inheritance would have occurred, if at all, in 1967 or 1971. Inter vivos trust distributions are not considered interests obtained "by bequest, devise, or inheritance." *In re Newman*, 903 F.2d 1150, 1153-54 & n. 3 (7th Cir.1990) (distinguishing and questioning *Smith v. Moody* (*In re Moody*), 837 F.2d 719, 723 & n. 12 (5th Cir.1988) and finding income payments to a beneficiary from an inter vivos trust do not qualify as interests obtained "by bequest, devise or inheritance."); *In re Kragness*, 58 B.R.

939, 944 (Bankr.D.Ore.1986). Mrs. Shurley's beneficial interest in the Trust does not qualify as inheritance.

B. To what extent, if any, is the power of appointment property of the estate?

The power of appointment granted Mrs. Shurley in the Trust did not become property of the bankruptcy estate, despite the fact that the power was exercisable inter vivos. Section 541(b)(1) excludes from property of the estate "any power that the debtor may exercise solely for the benefit of an entity other than the debtor." General powers of appointment, allowing a debtor to transfer trust assets to himself as well as others, are *included* in the property of the estate because they are not "solely" for the benefit of a non-debtor. Special powers of appointment, preventing the debtor from transferring trust assets to himself, are excluded from property of the estate. 4 LAWRENCE P. KING ET AL., COLLIER ON BANKRUPTCY ¶ 541.21 (15th ed. 1994).

Plaintiffs argue that "the type of appointment described in the Trust is not the type excluded under § 541(b) because such appointment would have a substantial impact on the assets of the Bankruptcy Estate." Plaintiffs imply that the Trust contains a general power of appointment, while the Shurleys contend that the power is special. The Trust provided that "[n]either Anne Bryant Ridge [Watkins] nor Jane Bryant Shurley can appoint assets to herself, her creditors, her estate, or the creditors of her estate." The language unequivocally allowed an appointment only in favor of lineal descendants of Mrs.

Shurley and Mrs. Watkins. The power is special and, hence, excludable from the property of the estate.

Plaintiffs further argue that any attempted exercise of the power would effectuate a post-petition transfer in violation of section 549. While this might be true, it does not bring the power of appointment into the property of the estate. Plaintiffs cite *Williams v. Chenoweth (In re Chenoweth)*, 132 B.R. 161, 166 (Bankr.S.D.Ill.1991), *aff'd*, 143 B.R. 527 (S.D.Ill.1992), *aff'd*, 3 F.3d 1111 (7th Cir.1993), in support. In *Chenoweth* the court found that the debtor's interest in her great-aunt's estate (1) was included in her bankruptcy estate and (2) a disclaimer of inheritance could be avoided by the trustee-in-bankruptcy under section 549. *Chenoweth* does not support the proposition that Mrs. Shurley's power of appointment is includable in her bankruptcy estate or that it cannot be exercised by Mrs. Shurley, but only that if Mrs. Shurley attempts to exercise her power, the trustee may avoid it.

Plaintiffs' assertion that it is "counter-intuitive" to allow the Trust assets to enter the bankruptcy estate while simultaneously allowing the "power" (to effectuate a transfer of those assets) to remain with the debtor is misplaced. A "power" can continue to exist despite the ineffectiveness of its exercise. In this case, all of Mrs. Shurley's interest in the M.D. Bryant Trust is property of her bankruptcy estate under section 541(a). Thus, Mrs. Shurley has no property left to appoint. While Mrs. Shurley has not lost the power to make such an appointment, her post-petition exercise of the power has been rendered meaningless.

C. Is injunctive relief proper?

Injunctive relief is proper because Plaintiffs have shown that they have no adequate remedy at law. To obtain preliminary injunctive relief, a movant must prove that:

(1) it is substantially likely to succeed on the merits,

(2) a substantial threat exists that the movant will suffer irreparable injury if the court does not grant the injunction,

(3) the threatened injury to the movant outweighs the threatened injury to the other party, and

(4) granting the injunction will not disserve the public interest.

Sierra Club, Lone Star Chapter v. FDIC, 992 F.2d 545, 551 (5th Cir.), *reh'g denied*, 3 F.3d 441 (5th Cir.1993). Where a movant seeks *permanent* injunctive relief, the second prong, irreparable harm, becomes a broader inquiry into the adequacy of any legal remedy. *Lewis v. S.S. Baune*, 534 F.2d 1115, 1123-24 (5th Cir.1976), *reh'g denied*, 545 F.2d 1299 (5th Cir.1977); 11 CHARLES A. WRIGHT & ARTHUR R. MILLER, FEDERAL PRACTICE AND PROCEDURE § 2944 at 399-401 (1973) (hereinafter referred to as WRIGHT & MILLER). Unlike the irreparable injury test, the inadequate remedy test looks to alternative modes of relief, however serious the initial injury, although often, irreparable harm alone is sufficient to satisfy this prong. *Lewis* at 1124. If movant does not succeed in carrying its heavy burden on any one of the four elements, the injunction may not issue. *Enterprise Int'l v. Corporacion Estatal Petrolera Ecuatoriana*, 762

F.2d 464, 472 (5th Cir.1985). The importance of each of these elements, however, may vary with the facts of each case. Courts apply a sliding-scale type balancing to two elements in particular, adjusting the likelihood of success on the merits by the gravity of the harm incurred, such that where, absent injunction, the harm is great to the plaintiff and insignificant to the defendant, the relative weight of the likelihood of plaintiff's success on the merits is diminished. *Canal Auth. v. Callaway*, 489 F.2d 567, 576-77 (5th Cir.1974); *see Cronin v. United States*, 919 F.2d 439, 445 (7th Cir.1990); *Roland Mach. Co. v. Dresser Indus.*, 749 F.2d 380, 387-388 (7th Cir.1984); 11 WRIGHT & MILLER § 2948; *see also Ohio Oil Co. v. Conway*, 279 U.S. 813, 815, 49 S.Ct. 256, 256-57, 73 L.Ed. 972 (1929) ("[w]here the questions presented by an application for an interlocutory injunction are grave, and the injury to the moving party will be certain and irreparable, if the application be denied and the final decree be in his favor, while if the injunction be granted the injury to the opposing party, even if the final decree be in his favor, will be inconsiderable, or may be adequately indemnified by a bond, the injunction usually will be granted").

Because Plaintiffs have been successful in this trial, the first element is established. The second element, balancing of the threatened injury to the Plaintiffs with the threatened harm to the Defendants, is also an easy matter, post-trial. The injury to the Plaintiffs is that the crown jewel of the bankruptcy estate, Mrs. Shurley's "interest" in the Trust, will be passed on to descendants if Mrs. Shurley successfully exercises her power of appointment. Plaintiffs would then be forced to recover bankruptcy

estate assets from Mrs. Shurley's descendants under section 549. The injury to Defendant Mrs. Shurley is that she will be denied her Trust-given right to appoint Trust assets to her descendants. Given that this Court has determined that the property over which Mrs. Shurley may exercise her power is property of her bankruptcy estate, it is easy to conclude that she would suffer no legal injury were an injunction to issue. Defendant Armstrong will also suffer no injury because Mrs. Shurley's interest in the Trust merely has another owner. It is also difficult to imagine how an injunction prohibiting distributions would disserve the public interest, since neither Mr. Armstrong nor Mrs. Shurley retains an equitable or legal right to Mrs. Shurley's beneficial interest in the Trust.

The more difficult question is whether a substantial risk exists that Plaintiffs will suffer irreparable harm without an injunction or whether an adequate remedy at law exists. Where an equitable remedy is sought, the harm may be irreparable. Where a legal remedy is available, however, the harm is generally not irreparable. *F.D.I.C. v. Faulkner*, 991 F.2d 262, 265 (5th Cir.1993). Moreover, as a general rule, an injunction is not appropriate to secure post-judgment legal relief in the form of damages. *De Beers Consol. Mines v. United States*, 325 U.S. 212, 219-23, 65 S.Ct. 1130, 1133-36, 89 L.Ed. 1566 (1945); *ITT Community Dev. Corp. v. Barton*, 569 F.2d 1351, 1360-61 (5th Cir.1978). Such an injunction would be in the form of a "prejudgment attachment" requiring compliance with FED.R.CIV.P. 64. *F.S.L.I.C. v. Dixon*, 835 F.2d 554, 561 (5th Cir.1987). This case, however, has proceeded beyond the

preliminary stage to judgment; post-judgment containment, not "pre-judgment attachment," is the issue. Moreover, the Fifth Circuit has shown a willingness to embrace an exception to this general rule where the facts indicate the collection of a money judgment would be rendered virtually impossible absent an injunction. *Dixon* at 560 n. 1 (citing *Tri-State Generation & Transmission Assoc. v. Shoshone River Power, Inc.*, 805 F.2d 351, 355 (10th Cir.1986)); *Enterprise Int'l*, 762 F.2d at 473 ("[t]he absence of an available remedy by which the movant can later recover monetary damages, however, may also be sufficient to show irreparable injury"); *see Ohio Oil Co. v. Conway*, 279 U.S. 813, 815, 49 S.Ct. 256, 256, 73 L.Ed. 972 (1929).

In this case, Plaintiffs' concern about the liquidation of available assets is persuasive. Under Texas law, Mr. Armstrong has a duty to carry out Mrs. Shurley's appointment of assets. If he does, TCB and other creditors will be unable to obtain satisfaction of significant claims from the bankruptcy estate. Although such an appointment might be recoverable from multiple appointees under section 549, there is no guarantee that such assets will not be dissipated by the respective appointees in anticipation of Plaintiffs' pursuit. The substantial obstacles Plaintiffs will face under section 549 in trying to collect widely dispersed assets serve to render that remedy "inadequate."

This conclusion is bolstered by cases finding the availability of money damages inadequate where the multiplicity of litigation would be necessary to collect such damages. *Foltz v. U.S. News & World Report*, 760 F.2d 1300, 1308 (D.C.Cir.1985) (remanding to allow the district court to enjoin employee benefits plan defendant from

paying out plan assets to its numerous recipients, because the court found that if plaintiffs had to chase the assets disbursed to plan participants, the plaintiffs might never recover); *Lynch Corp. v. Omaha Nat'l Bank*, 666 F.2d 1208, 1212 (8th Cir.1981) ("Lynch's injury is irreparable and there is no adequate remedy at law because a multiplicity of suits would be required to gain relief").

Finally, an injunction of this sort must be examined in light of bankruptcy policy. Cases disfavoring any sort of "pre-judgment attachment" generally are concerned about the "preference" given to one creditor over other creditors, a policy objective the Bankruptcy Code sought to avoid. The requested injunction would not favor one creditor over any other, but rather it would assure that trust assets, now property of the bankruptcy estate, would not be improperly transferred and would be available for unsecured creditors pro rata. The request is narrow in scope and limited in its application. It only asks for preservation of property of the bankruptcy estate by preventing transfers of property of the estate. The injunction also provides direction to the Trustee, who may perceive conflicting duties under Texas and federal law. The injunctive relief requested is warranted and will issue.

CONCLUSION

For the reasons stated in this Amended Opinion, Mrs. Shurley's one-half interest in the Trust does not qualify for spendthrift trust or discretionary trust protection which would exclude it from property of the estate. It is, therefore, property of the estate which must be turned

over to Mr. Elam, the Chapter 7 Trustee. In addition, Mr. Armstrong, the Trustee of the Trust, must be enjoined from disbursing any of the beneficial interests previously held by Mrs. Shurley to anyone other than Mr. Elam, the Chapter 7 Trustee.

This Amended Opinion constitutes the findings of fact and conclusions of law of this Court pursuant to FED.R.BANKR.P. 7052. This Amended Opinion also supersedes the Court's prior opinion, and amends the prior findings of fact and conclusions of law stated orally and in open court and recorded on the Record following the close of evidence. A separate Judgment has been rendered.

APPENDIX 3

SUBCHAPTER III – THE ESTATE

§ 541. Property of the estate

(a) The commencement of a case under section 301, 302, or 303 of this title creates an estate. Such estate is comprised of all the following property, wherever located and by whomever held:

(1) Except as provided in subsections (b) and (c)(2) of this section, all legal or equitable interests of the debtor in property as of the commencement of the case.

(2) All interests of the debtor and the debtor's spouse in community property as of the commencement of the case that is –

(A) under the sole, equal, or joint management and control of the debtor; or

(B) liable for an allowable claim against the debtor, or for both an allowable claim against the debtor and an allowable claim against the debtor's spouse, to the extent that such interest is so liable.

(3) Any interest in property that the trustee recovers under section 329(b), 363(n), 543, 550, 553, or 723 of this title.

(4) Any interest in property preserved for the benefit of or ordered transferred to the estate under section 510(c) or 551 of this title.

(5) Any interest in property that would have been property of the estate if such interest had been an interest of the debtor on the date of the filing of the petition, and that the debtor acquires or becomes entitled to acquire within 180 days after such date –

(A) by bequest, devise, or inheritance;

(B) as a result of a property settlement agreement with the debtor's spouse, or of an interlocutory or final divorce decree; or

(C) as a beneficiary of a life insurance policy or of a death benefit plan.

(6) Proceeds, product, offspring, rents, or profits of or from property of the estate, except such as are earnings from services performed by an individual debtor after the commencement of the case.

(7) Any interest in property that the estate acquires after the commencement of the case.

(b) Property of the estate does not include –

(1) any power that the debtor may exercise solely for the benefit of an entity other than the debtor;

(2) any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease before the commencement of the case under this title, and ceases to include any interest of the debtor as a lessee under a lease of nonresidential real property that has terminated at the expiration of the stated term of such lease during the case;

(3) any eligibility of the debtor to participate in programs authorized under the Higher Education Act of 1965 (20 U.S.C. 1001 et seq.; 42 U.S.C. 2751 et seq.), or any accreditation status

or State licensure of the debtor as an educational institution or[1]

(4) any interest of the debtor in liquid or gaseous hydrocarbons to the extent that –

(A) the debtor has transferred or has agreed to transfer such interest pursuant to a farmout agreement or any written agreement directly related to a farmout agreement; and

(B) but for the operation of this paragraph, the estate could include such interest only by virtue of section 365 or 544(a)(3) of this title.

Paragraph (4) shall not be construed to exclude from the estate any consideration the debtor retains, receives, or is entitled to receive for transferring an interest in liquid or gaseous hydrocarbons pursuant to a farmout agreement.

(c)(1) Except as provided in paragraph (2) of this subsection, an interest of the debtor in property becomes property of the estate under subsection (a)(1), (a)(2), or (a)(5) of this section notwithstanding any provision in an agreement, transfer instrument, or applicable nonbankruptcy law –

(A) that restricts or conditions transfer of such interest by the debtor; or

(B) that is conditioned on the insolvency or financial condition of the debtor, on the commencement of a case under this title, or on the appointment of or taking possession by a trustee in a case under this title or a custodian before

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[1] So in original. Probably should be "; or".

such commencement, and that effects or gives an option to effect a forfeiture, modification, or termination of the debtor's interest in property.

(2) A restriction on the transfer of a beneficial interest of the debtor in a trust that is enforceable under applicable nonbankruptcy law is enforceable in a case under this title.

(d) Property in which the debtor holds, as of the commencement of the case, only legal title and not an equitable interest, such as a mortgage secured by real property, or an interest in such a mortgage, sold by the debtor but as to which the debtor retains legal title to service or supervise the servicing of such mortgage or interest, becomes property of the estate under subsection (a)(1) or (2) of this section only to the extent of the debtor's legal title to such property, but not to the extent any equitable interest in such property that the debtor does not hold.